

UNITED STATES OF AMERICA 96 FERC ¶ 61,060
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Curt Hébert, Jr., Chairman;
William L. Massey, Linda Breathitt,
and Pat Wood, III.

PJM Interconnection, L.L.C. and
Allegheny Power

Docket No. RT01-98-000

Allegheny Power

Docket No. RT01-10-000

ORDER PROVISIONALLY APPROVING RTO PARTICIPATION
AGREEMENTS AND TARIFF CHANGES, AS MODIFIED,
AND DEFERRING CONSIDERATION OF PROPOSED RATE
CHANGES AND DISPOSITION OF FACILITIES

(Issued July 12, 2001)

On March 15, 2001, Allegheny Power (Allegheny) and the PJM Interconnection, L.L.C. (PJM) (collectively, Applicants) filed a joint proposal, pursuant to sections 203 and 205 of the Federal Power Act (FPA),¹ to comply with the Commission's order on Regional Transmission Organizations (RTOs).² Applicants' proposal would allow Allegheny to join the PJM RTO, as proposed by PJM in Docket No. RT01-2-000 (PJM RTO Filing). In addition, Allegheny proposes to assess certain transitional surcharges to recover the costs it claims it would incur in connection with its participation in the PJM RTO.

As discussed below, we will provisionally approve Allegheny's request to join the PJM RTO, subject to conditions. In a separate order to be issued concurrently, we direct

¹16 U.S.C. §§ 824b and 824d (1994).

²Regional Transmission Organizations, Order No. 2000, 65 Fed. Reg. 809 (January 6, 2000), FERC Stats. & Regs. ¶ 31,089 (1999), order on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (March 8, 2000), FERC Stats. & Regs. ¶ 31,092 (2000), petitions for review pending sub nom., Public Utility District No. 1 of Snohomish County, Washington v. FERC, Nos. 00-1174, et al. (D.C. Cir).

the participants in the proceedings involving the proposed Northeastern RTOs to participate in mediation on forming a single Northeastern RTO.³

The Commission has been attempting to facilitate the development of large, regional transmission organizations reflecting natural markets since we issued Order No. 2000. We favor the development of one RTO for the Northeast, one RTO for the Midwest, one RTO for the Southeast, and one RTO for the West. Through their independence from market participants, RTOs can ensure truly non-discriminatory transmission service and will instill confidence in the market that will support the billion of dollars of capital investment in generation and demand side projects necessary to support a robust, reliable and competitive electricity marketplace. RTOs are the platform upon which our expectations of the substantial generation cost savings to American customers are based.

While there will be "start up" costs in forming a larger RTO, over the longer term, large RTOs will foster market development, will provide increased reliability, and will result in lower wholesale electricity prices. However, these savings will be delayed, perhaps significantly, if RTOs are permitted to develop incompatible structures and systems, or if we approve RTOs that do not encompass wholesale market trading patterns. Accordingly, we today direct the parties in the Northeast and Southeast to mediation, under an expedited schedule.

Background

A. Allegheny and PJM

Allegheny comprises three operating companies: Monongahela Power Company, the Potomac Edison Company, and West Penn Power Company. Its service territory is located in the States of Maryland, Ohio, Pennsylvania, Virginia, and West Virginia. Allegheny currently serves a summer peak load capacity of 7,788 MW, and is a member of the East Central Area Reliability Coordination Agreement (ECAR).

PJM operates the largest, centrally dispatched control area in North America, with a service area that includes all or part of Pennsylvania, New Jersey, Maryland, Delaware, Virginia, and the District of Columbia. PJM has a pooled generating capacity of over

³See also PJM Interconnection, L.L.C., et al., 95 FERC ¶ 61,___ (2001) (PJM RTO Order); New York Independent System Operator, Inc., et al. 95 FERC ¶ 61. ___ (2001); Bangor Hydro-Electric Company, et al., 95 FERC ¶ 61,___ (2001).

58,000 MW and is member of Mid Atlantic Area Council (MAAC). On January 1, 1998, PJM began operation as an independent system operator (ISO).⁴ As noted above, the Commission is provisionally granting PJM RTO status in the PJM RTO Order issued today.

B. Applicants' Proposal

1. PJM West

Applicants' propose to transfer the operational control of their jurisdictional transmission facilities currently owned and operated by Allegheny to the PJM RTO, effective January 1, 2002.⁵ Under Applicants proposal, Allegheny's transmission facilities would become subject to PJM's open access transmission tariff (PJM OATT). Allegheny would also participate in a regional transmission expansion plan and would be required to coordinate its transmission facility maintenance through PJM. Applicants

⁴See Pennsylvania-New Jersey-Maryland Interconnection, et al., 81 FERC ¶ 61,257 (1997), order on reh'g, 92 FERC ¶ 61,282 (2000).

⁵Applicants' proposal was previously addressed by Allegheny, on October 16, 2000, in Allegheny's initial RTO compliance filing in Docket No. RT01-10-000. In that filing, Allegheny reported that it had not yet determined whether it would seek membership in the proposed Alliance Companies (Alliance) RTO or the proposed PJM RTO. Allegheny stated, however, that a hybrid arrangement between itself and PJM, which it called "PJM West," could combine the best features of the Alliance RTO and the PJM RTO. Accordingly, Allegheny requested Commission guidance as to whether the PJM West concept would satisfy the requirements of Order No. 2000. Allegheny explained that the basic features of the PJM West concept were set forth in a memorandum of agreement (MOA) executed between Allegheny and PJM. The MOA provided that Allegheny would become subject to the PJM transmission owners agreement and the PJM operating agreement, but that Allegheny and PJM would negotiate a new reliability assurance agreement. In addition, the MOA contemplated the formation of PJM West as an independent transmission company (transco) within PJM. The MOA also committed the parties to addressing Allegheny's revenue losses associated with the elimination of pancaked rates, by way of a revised Alliance RTO region wide rate for through and out transactions. On February 7, 2001, Allegheny filed a withdrawal of its petition for declaratory order, noting that it had incorporated a new rate proposal consistent with the Commission's rulings addressing the Alliance RTO. That rate proposal is addressed below.

state that to the greatest extent possible, PJM West would be operated and controlled by PJM using the same rules, terms and conditions that currently apply within PJM.

Applicants state, however, that because PJM West and PJM would be subject to different reliability councils (PJM is a member of MAAC, while Allegheny is a member of ECAR), PJM West would be required to follow ECAR's reliability guidelines. Consequently, PJM West would use a different reserve requirement methodology than the existing PJM load serving entities (LSEs).

Included in Applicants' filing are the basic agreements establishing PJM West, including (i) the PJM West Implementation Agreement (Implementation Agreement); (ii) the West Transmission Owners Agreement among PJM Interconnection, L.L.C. and Certain Owners of Electric Transmission Facilities (West TOA); and (iii) the PJM West Reliability Assurance Agreement (West RAA). Applicants state that the expansion of PJM West also requires amendments to the PJM OATT, the PJM Operating Agreement, and the PJM Transmission Owners Agreement.

2. Allegheny's Rate Proposals

Allegheny also sponsors a transition rate increase mechanism, which it submits pursuant to section 205 of the FPA. Allegheny states that its rate request is designed to recover two separate expenses. First, it would allow Allegheny to recover the transmission revenues it projects it would lose once it eliminates the rate pancaking between its system and PJM. Second, it would permit Allegheny to recover the start-up expenses it projects its will incur once it joins PJM. These costs would be recovered by Allegheny through transitional surcharges on all through or out firm and non-firm point-to-point service. In addition, Allegheny also proposes a separate transitional surcharge on megawatt hours of energy received into its system by generators and delivered from its system to loads.

C. Notices and Responsive Pleadings

Notice of Applicants' filing was published in the Federal Register,⁶ with interventions, comments, or protests due on or before April 20, 2001. Notices of intervention and motions to intervene were submitted by the entities listed in Appendix to this order. Protests and comments were filed by the parties noted below in the discussion section of this order, and as also noted in Appendix. A request to consolidate

⁶66 Fed. Reg. 2424, 8578 (2001).

Docket No. RT01-98-000 with PJM's RTO filing in Docket No. RT01-2-000 was made by FirstEnergy Corp. (First Energy).

On May 8, 2001, Applicants filed an answer to protests addressing, among other things, Applicants' proposed mechanisms for ensuring reliability within the PJM and PJM West regions, and Allegheny's rate proposals. Applicants also oppose FirstEnergy's request for consolidation, claiming that it is unnecessary.⁷

Answers were also filed on May 18, 2001 by the City of Hagerstown, Maryland, the Town of Thurmont, Maryland, the Town of Williamsport, Maryland and the Town of Front Royal, Virginia (Municipalities), and on May 22, 2001, by Allegheny Electric Cooperative and Old Dominion Electric Cooperative (AEC, et. al.)

Discussion

A. Procedural Matters

Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,⁸ the notices of intervention and the timely, unopposed motions to intervene submitted by the entities noted in Appendix serve to make these entities parties to this proceeding. In addition, we will accept the unopposed late-filed intervention submitted by AES New Energy Inc., Public Service Electric and Gas Company, PSE&G Power LLC, PSE&G Energy Resources & Trade LLC, and the Public Utilities Commission of Ohio.⁹

⁷FirstEnergy's motion to consolidate was also opposed by PPL Electric Utilities Corporation (PPL) in an answer submitted on May 7, 2001.

⁸18 C.F.R. § 385.214 (2000).

⁹Notice of Allegheny's filing in Docket No. RT01-10-000 was also published in the Federal Register, 65 Fed. Reg. 64,214 (2000), with interventions, comments, or protests due on or before November 20, 2000. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, the notices of intervention and the timely, unopposed motions to intervene submitted by the entities noted in Appendix to this order serve to make these entities parties to this proceeding. In addition, we will accept the unopposed late-filed intervention submitted by the Pennsylvania Commission and the Maryland Commission.

Rule 213(a) of the Commission's Rules of Practice and Procedure,¹⁰ prohibits an answer to a protest and an answer to an answer, unless otherwise permitted by the decisional authority. We will accept the answer to protests filed by Applicants, AEC, et al., and Municipalities, given the complex nature of this proceeding and because these answers aided in clarifying certain issues, as discussed below.

As requested, we will grant Allegheny's motion to withdraw its petition for declaratory order in Docket No. RT01-10-000, and hereby terminate that proceeding. We will deny FirstEnergy's motion to consolidate Docket Nos. RT01-98-000 and RT01-2-000.

B. Independence

1. Applicants' Proposal

In Order No. 2000, we held that an RTO must be independent of any market participant.¹¹ Applicants state that the PJM West proposal satisfies this requirement for the same reasons relied upon by PJM in the PJM RTO Filing. As a member of PJM, Applicants state that Allegheny would generally have the same rights and responsibilities as PJM's existing members.

With respect to governance matters relating to reliability concerns, Applicants propose a reliability agreement for PJM West, the West RAA, which would operate independently of PJM's reliability agreement.¹² Under the West RAA, Applicants propose to establish a Reliability Committee for PJM West which would comprise all LSEs in the PJM West region. The Reliability Committee would manage the West RAA, while PJM would be responsible for administrative duties and for the assurance of the short-term reliability of grid operations within the PJM West region.

2. Responsive Pleadings

Reliant Energy Northeast Generation, Inc. (Reliant), Edison Mission Energy and Edison Mission Marketing & Trading, Inc. (Edison), and Orion Power Midwest, L.P.

¹⁰18 C.F.R. § 385.213(a)(2) (2000).

¹¹Order No. 2000 at 31,061.

¹²See Reliability Assurance Agreement Among Load-Serving Entities in the PJM Control Area (RAA).

(Orion) question whether the West RAA satisfies the Commission's independence standard. Edison and Orion argue that the governance provisions under the West RAA should be expanded to include generators and other stakeholders.

Strategic Energy L.L.C. (Strategic), Mid-Atlantic Power Supply Association (MAPSA), AEC, et al. argue that Applicants' proposals were not the product of a collaborative PJW-wide stakeholder process. MAPSA contends that while stakeholders in the MAAC region were involved in this process, stakeholders in the ECAR region were not. MAPSA also asserts that neither the West RAA nor the West TOA were approved by the committees within PJM that have responsibility over these matters. AEC, et al. object to the need for the separate operating documents giving rise to PJM West.

3. Applicants' Answer

In response to the charge that the collaborative process leading up to Applicants' PJM West proposal was inadequate, Applicants state that the success of their efforts was confirmed by the results produced. Specifically, Applicants state that the changes to PJM Operating Agreement were approved by an overwhelming margin and that the changes to the PJM OATT were approved by acclamation. Applicants deny that Allegheny had undue influence in the proposal process, stating that PJM and Allegheny needed to develop the draft business terms in which both parties were willing to move forward under a joint RTO. Applicants deny that Allegheny could have undue influence in the future since Allegheny will have the same rights and responsibilities as any other PJM member under the PJM Operating Agreement.

In response to the charge that the governing body under the West RAA would be too limited, Applicants state that broader stakeholder participation is currently being considered within PJM. Applicants state that certain market-type rules could be transferred from the West RAA to the PJM Operating Agreement, which is governed by a broader group of market participants.

4. Discussion

We find that Applicants' proposal generally satisfies the Commission's RTO independence requirement, consistent with our finding today in the PJM RTO Order. Applicants' proposed expansion of PJM to include Allegheny would not affect PJM's ability to act independently of market participants.

Regarding Reliant and Edison's argument regarding the West RAA, we agree with intervenors that no one stakeholder group should have control over the RTO's reliability decisions. Through the West RAA, LSE's have exclusive responsibility for determining reliability requirements that affect PJM's energy markets. For the same reasons discussed in the PJM RTO Order regarding PJM's RAA, therefore, we will require that the PJM Board, which is independent of market participants, have exclusive authority to propose changes to reliability requirements under section 205 of the FPA. The Reliability Committee's role in establishing reliability requirements must therefore be advisory to the PJM Board. Finally, PJM should review the feasibility of expanding the membership of the Reliability cCommittee under the West RAA to include participants other than LSEs.

We reject the protest arguments concerning the collaborative process leading up to the Applicants' filing. To the extent these arguments address the substantive provisions of Applicants' filing, we will address these issues, below, in the specific context in which they arise.

C. Scope and Regional Configuration

In Order No. 2000, we held that an RTO must serve an appropriate region, i.e., a region of sufficient scope and configuration to permit the RTO to effectively perform its required functions and to support efficient and non-discriminatory power markets.¹³ Applicants claim that the PJM West proposal satisfies this requirement, given the fact that PJM would be significantly expanded. Applicants point out that the expanded PJM would operate over 13,000 miles of transmission lines over a 79,000 square mile service territory, and would include over 590 generating units with a generation capacity of 66,070 MW.¹⁴ Applicants state that with the inclusion of PJM West, PJM's scope and regional configuration will be significantly enhanced.

Intervenors generally concur. Mirant Americas Energy Marketing, LP, et al. (Mirant), for example, state that the expansion of PJM will help promote the goals of a uniform set of standard market rules across the entire Northeast and Mid-Atlantic regions, and that the single-market, multiple control area model should serve as a

¹³Order No. 2000 at 31,076.

¹⁴In addition, PJM describes the interconnection between PJM West and existing PJM as at least as strong as the interconnections between many of the existing PJM transmission owners with four 115-kV interconnections, two 138-kV interconnections, eight 230-kV interconnections and three 500-kV interconnections, with a total transmission capability of 13,000 megawatts.

template for establishing uniform market rules across all of the Northeastern ISOs. The Virginia State Corporation Commission (Virginia Commission) characterizes Applicants' scope and regional configuration as a positive step forward, while the Pennsylvania Office of Consumer Advocate (Pennsylvania OCA) emphasizes the importance of adding additional facilities and load to the generally successful wholesale market currently being operated by PJM.

We agree with the intervenors' comments regarding the expansion of PJM. As we note today in the PJM RTO Order; however, the market in which PJM does business is a market which significantly exceeds PJM's existing boundaries, even including the Allegheny system. This market, moreover, is a balkanized market that would be better served by a single RTO. In the PJM RTO Order, we conclude that PJM's proposed scope and regional configuration represents a platform that can and should be expanded upon. We also encourage the three existing Northeast ISOs to look at the best practices in all three ISOs and to adopt those market rules that would be appropriate for a single Northeast RTO. In order to successfully encompass the natural market for bulk power in the Northeast, it is necessary that the Northeast transmission owners combine to form a single RTO.

Consistent with this ruling, and in consideration of the above, we are issuing concurrent with this order, a separate order that directs the participants in this proceeding and the participants in Docket Nos. RT01-2-000 (PJM), RT01-95-000 (New York) and RT01-86-000 and RT01-94-000 (New England), to participate in settlement discussions for 45 days before a mediator and appropriate consultants to assist and provide advice during the mediation. The order directing mediation requires the mediator to file a report within 10 days after the 45 day period, which includes an outline of the proposal to create a single Northeastern RTO, milestones for completion of intermediate steps and a deadline for submitting the joint proposal.¹⁵ We intend to review the report and may issue a subsequent order.

We encourage the state commissions to participate in these efforts. We believe their participation will further the resolution of this matter. Similarly, we encourage Canadian entities that are part of the Northeast Power Coordinating Council to participate in the discussions to the extent consistent with their status as subjects of a foreign sovereign nation.

¹⁵Alternatively, should Allegheny determine that its interests would be better served by its participation in the Alliance RTO, such a commitment should also be developed in concrete terms as expeditiously as possible.

D. Operational Authority

In Order No. 2000, we found that an RTO must have operational authority for all transmission facilities under its control.¹⁶ Applicants state that PJM will direct the operation of PJM West transmission assets through PJM's central control center while the physical control of these assets will remain with the transmission owners. PJM's operational authority over PJM West assets would include directing switching of transmission facilities, monitoring and controlling real and reactive power flows, monitoring and controlling voltage levels and scheduling and operating reactive resources. PJM's maintenance schedules for generation and transmission would be used by the transmission owners to coordinate maintenance of their facilities. PJM would exercise NERC security coordinator functions for PJM West within the rules of ECAR. We find that Applicants' proposal satisfies the Commission's operational authority requirement.

E. Short-Term Reliability

1. Applicants' Proposal

In Order No. 2000, we held that an RTO must have exclusive authority for maintaining the short-term reliability of the grid that it operates.¹⁷ Applicants state that the PJM West proposal satisfies this requirement because PJM would have the same responsibility for short-term reliability that it currently has, including the same authority to order redispatch, the same authority as to transmission and generator maintenance coordination, the same role as to facility ratings, and the same commitment to abide by relevant reliability standards.

Applicants note, however, that to ensure short-term reliability over PJM West, PJM would be required to coordinate generation and transmission operations over multiple control areas and over the geographical expanse of two regional reliability councils: MAAC for the existing control area and ECAR for PJM West.

Applicant's state that both MAAC and ECAR share the same reliability standard, i.e., a one-day-in-ten-years loss-of-load expectation. However, the reserve requirements

¹⁶Order No. 2000 at 31,086.

¹⁷Id. at 31,092.

used to meet this reliability standard differ between the two councils.¹⁸ Applicants state that in order to facilitate a single regional energy market across both reliability regions, they are proposing reserve rules which they claim are compatible. Specifically, the West RAA would require LSEs to maintain available reserves (including generating resources that could be made available on up to four hours notice and loads that could be interrupted on up to two hours notice) of 106 percent. Applicants claim that this available capacity (ACAP) requirement would be comparable to PJM's use of an installed capacity (ICAP) margin of 119 percent of the forecast annual peak load.¹⁹

Under the West RAA, PJM would administer the PJM West ACAP requirement by imposing a daily available capacity obligation (DACO). The DACO for each LSE would be 106 percent of the total day ahead estimated load requirement coincident with the zone peak for that LSE in PJM West. Should the LSE either fail to specify its resources, or specify, but fail to meet its obligation, the necessary amount of DACO would be purchased by PJM from the available capacity credit market. In the event of a shortfall due to an insufficiency of bid offers, the LSE would be subject to a deficiency charge, unless the shortfall arose because of an unexpectantly high load.

The proposed deficiency charge would be \$11,860 per MW of deficiency per day.²⁰ Revenues attributable to the collection of this deficiency charge would be distributed by PJM on a megawatt basis for the day for which the deficiency was assessed, to the LSEs which provided sufficient available capacity to meet the DACO.

Applicants also propose an alternative deficiency charge which could be elected by an LSE for any forecast period by giving notice of such election no later than one

¹⁸MAAC requires LSEs to have an installed reserve margin of 19 percent of their forecast annual peak load. This margin is set annually on a two-year forward basis where installed capacity is reduced by the 12-month rolling-average forced outage rate of the resource. ECAR, by contrast, requires LSEs to have an operating reserve margin, *i.e.*, installed resources that are available within 10 minutes or less, set at 4 percent of the LSE's forecast hourly peak load for the next day (this margin includes load and frequency regulation (spinning) reserves, contingency spinning reserves, and contingency supplemental reserves).

¹⁹Applicants explain that under the RAA, the installed reserve margin is set annually on a two-year forward basis.

²⁰The proposed charge is based on the annual costs of a combustion turbine generator divided by five annual peak days.

month prior to the start of the forecast period. If an LSE designates accredited net capacity to meet its obligations per PJM's installed reserve margin, then an effective charge of \$177.30 per MW-day ($\$160\text{MW} / (1 - \text{pool forced outage rate})$) would be levied against an LSE with deficient operating reserves.²¹

2. Responsive Pleadings

PPL and Duke argues that Applicants' stated objective for the differing reserve requirements is comparability, but that the degree of comparability between the PJM West standard and the PJM standard has not been supported. PPL further maintains that because the reserve requirements differ, generating units in PJM West should not be certified as equivalent capacity for PJM unless certification is pursuant to the existing rules in PJM. PPL is also concerned that the same capacity could be used to meet reliability requirements simultaneously in both regions, thus negatively impacting reliability.

Duke Energy North America, LLC (Duke) questions how Applicants' proposed level of reserves available within four hours would ensure coverage for ECAR's operating reserves requirement. PPL, Orion, and Duke also question why PJM's ICAP requirement was not chosen as the uniform reliability requirement for both PJM West and PJM. PPL argues that this measure would be superior due to the greater stability of the MAAC region.

Conversely, numerous intervenors (e.g., FirstEnergy, GPU Energy (GPU), and Enron Power Marketing, Inc. (Enron)) argue the superiority of the existing ECAR operating reserve requirement. Enron prefers the operating reserve requirement similar to the ECAR requirement and states that an installed capacity requirement was needed when power prices were regulated. However, because market prices for energy and reserves provide the appropriate signals for new investment to occur, an operational reserve requirement satisfies reliability concerns. Strategic asserts that the 106 percent requirement would be anti-competitive requiring market entrants to incur out-of-pocket expenses while Allegheny would not. FirstEnergy states that if LSE's incur additional financial obligations in order to meet ACAP, the LSE's should be grandfathered and held harmless from any adverse impact of the imposition of ACAP.

²¹LSEs would also be required to provide related planning information and firm transmission capacity for the installed capacity and to maintain and not delist the installed capacity to qualify for this reduced charge.

With respect to the deficiency charge, AEC, et al. believe that the \$11,680/MW-deficiency day represents a dramatic increase in costs for LSEs in PJM West over the current \$12.13/MW-deficiency day, while there has been no showing of the need for this change nor the benefit in increased reliability in ECAR over the model currently in place. MAPSA and AEC, et al. contends that the charge is unjust and unreasonable. FirstEnergy questions the ability of transmission customers to mitigate their risks of paying the deficiency charge of \$11,680/MW-day via the capacity benefit margin (CBM). PPL and FirstEnergy contend that Applicants' filing fails to address the relationship between CBM and the available capacity obligation in sufficient detail. FirstEnergy states that it is opposed to any proposal that would reduce ATC between Allegheny and itself by application of the PJM CBM calculation to PJM West.

3. Applicants' Answer

Applicants agree that a uniform reliability standard should apply throughout the RTO and that discussions to find an alternative to ICAP for the existing PJM area can now include ECAR stakeholders such that a long-term solution can be adopted. Applicants state, however, that their proposed ACAP requirement was designed to make reliability rules for PJM West compatible with the rest of PJM; thus precluding one area from unfairly "leaning" on the other and thus allowing a single clearing energy price for the entire region (versus one region's energy price having a capacity component and the other being free of that component).

In response to PPL's concerns regarding the possibility of double-counting commitment of capacity, Applicants state that resources can only commit at a given time to be either capacity resources under the RAA or Available Capacity Resources under the West RAA. In addition, Applicants submit work papers from a 1999 working group which identified a daily 107.3 percent ACAP requirement as being comparable to a 120 percent ICAP requirement. Applicants state that the 107.3 percent requirement was based on estimated values for load and outages whereas PJM West will use actual figures.

PJM proposes to maintain its current method of calculating CBM, states that the only change will be the geographic area covered and commits to update its OASIS as required. PJM expects that it will be able to reduce the CBM at its expanded borders because the expanded PJM region will encompass a greater amount, and more diverse mix, of generation resources compared to the current PJM. However, PJM states that consistent application of CBM may result in changes to the Allegheny-FirstEnergy available transmission capacity (ATC).

4. Discussion

We find that the PJM West proposal generally satisfies the Commission's short-term reliability requirement, subject to the conditions discussed below. While we agree that a single reserve requirement for short-term reliability is ideal, we have previously held that an RTO may establish operating requirements that allow continuation of differences between reliability regions as long as NERC requirements are met.²² The choice of which reserve requirement(s) best ensure(s) short-term reliability should remain with the RTO, and market participants.

We reject intervenors' argument that the 106 percent available capacity requirement is anti-competitive because certain market entrants may have to incur costs to participate in the market. Strategic's argument is based on the level of the deficiency charge (i.e., the charge is so high that it will prevent new market entrants) and is moot; because, as discussed below, we reject the proposed charge and direct Applicants to devise a new deficiency charge.

The proposed deficiency charge is based on recovery of the annual costs of a combustion turbine generator over five annual peak days. We are concerned that an LSE would incur more than the annual costs used in the charge, if the LSE failed to comply with its daily obligation more than the number of annual peak days. Accordingly, we will reject Applicants' proposed deficiency charge. Finally, we are not persuaded that LSE's that commit reserves using available capacity should see a higher deficiency charge than LSE's that commit reserves using installed capacity. Once PJM has established a new deficiency charge, PJM should file that deficiency charge together with any necessary mitigation measures.

Schedule 6, Section 2.(n) of the West RAA states that procedures will be established that will enable the ability of resource owners to use CBM to replace available capacity resources with equivalent available capacity resources external to the PJM West region. We note in that PJM will retain its current CBM methodology and commits to apply it consistently and to post all required information on its OASIS site.

F. Tariff Administration and Design

²²Alliance Companies, et al., 89 FERC ¶ 61,298, 61,923 (1999) (Alliance I), order on compliance filing and reh'g, 91 FERC ¶ 61,152 (2000), order on compliance filing and reh'g, 94 FERC ¶ 61,070 (2001) (Alliance III), order denying reh'g and providing clarification, 95 FERC ¶ 61,182 (2001) (Alliance IV).

In Order No. 2000, we held that an RTO must administer its own transmission tariff and employ a transmission pricing system that will promote efficient use and expansion of transmission and generation facilities.²³ Applicants state that the PJM West proposal satisfies this RTO function. Under the terms of the interim coordination agreement previously approved by the Commission, Applicants state that PJM would be responsible for handling all transmission service and generation interconnection requests, and would integrate the Allegheny and PJM request queues into a single queue by January 1, 2002.²⁴

We find that the PJM West proposal generally satisfies the tariff administration and design requirements of Order No. 2000, subject to the conditions discussed below. Reliant Energy expresses concerns regarding PJM's responsibility for conducting service study requests and requests the Commission condition any acceptance on a requirement that such studies be completed either by PJM or an independent consultant. MAPSA questions whether PJM, and by extension PJM West, would be independently responsible for generation interconnection study requests. In the PJM RTO Order, issued today, we require PJM to revise the PJM OATT to provide that third parties be given sufficient information to conduct independent interconnection analyses and studies when requested to do so. The PJM RTO would retain the final decision-making authority over interconnection requests. The Commission also intends to evaluate in the near future the importance of standardizing interconnection policies and procedures.

G. Congestion Management

In Order No. 2000, we held that an RTO must ensure the development and operation of market mechanisms to manage transmission congestion.²⁵ Applicants state that the PJM West proposal satisfies this RTO function because it would require PJM to apply its currently effective congestion management system to PJM West.

The Borough of Chambersburg, Pennsylvania (Chambersburg) protests this feature of the PJM West proposal, arguing that Applicants' filing provides no information about the implications of applying the PJM locational marginal pricing

²³However, PJM would remain responsible for notifying the Commission of any conflicting standards that would hinder its ability to provide reliable, non-discriminatory and efficiently-priced transmission service. See Order No. 2000 at 31,106.

²⁴Allegheny Power Service Corporation, 95 FERC ¶ 61,045 (2001).

²⁵Order No. 2000 at 31,108.

system to entities in the PJM West region. Chambersburg requests that the Commission require Allegheny and PJM to provide this information to interested parties for review and comment. DMEC comments that it would like assurance that the allocation or auctions of firm transmission rights (FTRs) in the PJM West area will cause no harm to the allocation of FTRs in the original PJM ISO territory. The Virginia Commission notes that the PJM West operating agreement gives PJM West transmission owners the right to create and sell supplemental allocations of FTRs for transmission capacity over and above the amount allocated by PJM, subject to the transmission owner's own financial risk and responsibility for assuring firmness. The Virginia Commission proposes that the sale of such FTRs be authorized on an experimental basis only.

PJM will apply the same locational-marginal-price (LMP) congestion management system to the expanded area. We find that this proposal satisfies the congestion management function set forth in Order No. 2000. In the PJM RTO Order, issued today, we reiterate that while LMP is an acceptable approach for congestion management, the Commission does not prescribe any particular congestion management method. Nonetheless, varying congestion management systems within a natural market such as the greater Northeast can operate as a barrier to entry to new market participants. This is why it is critical for the market participants in the greater Northeast to reach agreement on market rules.

H. Parallel Path Flow

In Order No. 2000, we found that an RTO must develop and implement procedures to address parallel path flow issues within its region and with other regions no later than three years after it commences initial operation.²⁶ Applicants state that the PJM West proposal satisfies this RTO function because PJM would operate the control areas at issue as a virtual single control area, with a single energy market and congestion management system. PJM would internalize parallel path flows from all transactions between companies in the combined PJM/PJM West region.

We find that the PJM West proposal generally satisfies the parallel path flow requirements set forth in Order No. 2000, subject to conditions. While Applicants' proposal represents an important step toward addressing parallel path flows on an intra-regional basis, Applicants have yet to address how parallel flows will be internalized within the Northeast region and other regions to the west and south. Consistent with our findings as to scope and configuration, as set forth in the PJM RTO Order, therefore, we

²⁶Id. at 31,128.

direct Applicants to consider all appropriate procedures for addressing parallel flow issues on this broader level in compliance filing to be made within 60 days of the date of this order.

I. Ancillary Services

In Order No. 2000, we found that an RTO must serve as a provider of last resort of all ancillary services required by Order No. 888 and subsequent orders.²⁷ Applicants state that the PJM West proposal satisfies this RTO function because PJM West would generally rely on the same market structure for ancillary services as has been proposed by PJM, subject to certain modifications. Applicants state that the PJM West and PJM control areas would be individually responsible for any ancillary service costs whenever generation resources are used to satisfy regulation needs in that particular area. In effect, PJM and PJM West would pursue separate markets for ancillary services, with each area having its own regulation objectives.

In addition, Applicants state that they would initially adopt cost-based pricing for these services when operation begins in PJM West. Applicants indicate that initial discussions have taken place to establish a spinning reserve market by the summer of 2002, at which time, regulation would be subject to market based pricing.

Orion states PJM West's cost-based pricing for regulation service is too restrictive and asserts that such a structure allows for little consistency between the PJM and PJM West control areas. Orion proposes a price cap that would fluctuate according to the market price for regulation service as established in PJM. Orion argues that this price cap should be the maximum of the cost-based rate, as described in PJM-West's proposal, and the prevailing market price for regulation set in the PJM. This, they argue, better links the two RTO's and retains some incentive for generators to bid into the PJM West regulation market.

We find that the PJM West proposal satisfies the ancillary services requirements set forth in Order No. 2000. Much of the analysis provided by PJM and comments received regarding the proposed structure of its control area apply equally to that of PJM West due to the similarities between the market structures of the two areas. As we noted in PJM's RTO Order, PJM operates a reliable ancillary services market.

²⁷Id. at 31,130.

While we would prefer a single ancillary services market covering both PJM and PJM West, we find the segmented markets proposed by Applicants to be a reasonable feature to ensure a reliable service. Though acceptance of this structure is not predicated on future plans to establish a competitive marketplace in which ancillary service prices are freely set, the Commission encourages PJM West to continue their efforts of creating such a market in the near future.

We will defer ruling on Orion's request for a floating cost-of-service cap on ancillary services tied to market prices in PJM. When proposed rates are filed for these services, Orion may renew its protest at that time.

J. OASIS, Total Transmission Capability, and Available Transmission Capacity

In Order No. 2000, we held that an RTO must be the single OASIS site administrator for all transmission facilities under its control and independently calculate total transmission capability (TTC), and ATC.²⁸ Applicants state that PJM would operate a single OASIS site for the expanded PJM/PJM West region and would independently calculate TTC and ATC. Applicants also state that PJM will modify its existing e-business tools to accommodate the PJM West market participants and would add new features and capabilities to administer the new capacity and regulation markets in the west. We find that Applicants' proposal satisfies the OASIS requirements of Order No. 2000, for the same reasons, and subject to the same conditions, discussed in the PJM RTO Order.

K. Market Monitoring

In Order No. 2000, we held that to ensure that the RTO provides reliable, efficient, and not unduly discriminatory transmission service, the RTO must provide for objective monitoring of the markets it operates or administers to identify market design flaws, market power abuses and opportunities for efficiency improvements, and propose appropriate actions.²⁹ Applicants state that the PJM West proposal satisfies this requirement because their proposal would follow the same market monitoring structure as that proposed by PJM and previously accepted by the Commission as meeting the

²⁸Id. at 31,142.

²⁹Id. at 31,146.

requirements of Order No. 2000.³⁰ We find that the PJM West proposal satisfies the market monitoring requirements of Order No. 2000, for the same reasons discussed in our order addressing PJM's RTO compliance filing.³¹ The Commission has the statutory responsibility to ensure that public utilities selling competitive bulk power markets do not engage in market power abuse and also to ensure that markets within the Commission's jurisdiction are free of design flaws and market power abuse. To that end, the Commission will expect to receive reports and analyses of an RTO's market monitor at the same time they are submitted to the RTO.³² The Commission intends to work with the market monitor to ensure that markets are functional and free of abuse or design flaws.

L. Planning and Expansion

In Order No. 2000, we held that an RTO must be responsible for planning, and for directing or arranging necessary transmission expansions, additions, and upgrades that will enable it to provide efficient, reliable and non-discriminatory transmission service, and to coordinate such efforts with the appropriate state authorities.³³ Applicants state that PJM West satisfies this requirement, given its reliance on PJM's previously approved planning and expansion process.

We find that as part of an expanded PJM, the PJM West proposal generally satisfies the planning and expansion requirements set forth in Order No. 2000. Centralized planning and expansion activities, we have held, can promote the development of a competitive bulk power market by expanding trading opportunities, better integrating transmission grids, and alleviating regional congestion.

We emphasize that RTO regional transmission expansion plans must be more than a collection of traditional expansion plans developed by individual transmission owners to serve their needs. Instead, these plans should be developed with input from all appropriate participants. At the same time, it must be PJM who shoulders the ultimate responsibility for developing the plan and conducting all necessary studies and analyses.

³⁰PJM Interconnection, L.L.C., 86 FERC ¶ 61,247 (1999).

³¹PJM RTO Order at _____ .

³²California Independent System Operator Corporation, 86 FERC ¶ 61,059 (1999).

³³Order No. 2000 at 31,157.

M. Interregional Coordination

In Order No. 2000, we held that an RTO must ensure the integration of reliability practices within an interconnection and market interface practices among regions.³⁴ Applicants state that the establishment of PJM West satisfies this RTO function and represents a major step forward in interregional coordination. Applicants state that presently, their respective systems are located in separate control areas, and operate under separate security coordinators and reliability councils. Applicants state that under their proposal, the seams created by these boundaries will either be eliminated or overcome. In addition, Applicants state that PJM and the sponsors of the Alliance RTO have initiated an interregional coordination process.

FirstEnergy argues that Applicants' proposals have not done enough to address or resolve seams issues, including the seams issues between PJM and the Alliance RTO. First Energy proposes that Applicants be required to submit an executed agreement outlining its commitment to resolving these issues. In their answer, Applicants respond that they have asked Alliance for a list of seams issues which they have not received to date. Applicants further respond that they are committed to negotiations with Alliance once negotiations between Alliance and the Midwest ISO are complete.

With respect to issues raised concerning the combining of PJM with NYISO and ISO-NE, and seams issues in the Northeast region, these issues have been addressed in the Scope and Regional Configuration section of this order. In the PJM RTO Order issued today, we find that PJM's commitment to form PJM West is a step towards ensuring the integration of reliability practices to the west of PJM. However, Applicants have not yet developed a schedule with other transmission systems contiguous to their facilities, such as Alliance and GridSouth, to address seams issues. To ensure the integration of reliability and market interface practices to the south and west, it is necessary that Applicants coordinate their transmission practices with these entities.

N. Open Architecture

In Order No. 2000, we held that any proposal to participate in an RTO must not contain any provision that would limit the capability of the RTO to evolve in ways that

³⁴Id. at 31,167.

would improve its efficiency, consistent with the required characteristics and required function for an RTO.³⁵

Applicants state that under the West TOA, some or all of the PJM West transmission owners could seek to form an independent transmission company (ITC) in the future. The West TOA establishes this as "Phase II" of PJM West to allow time for the initial establishment of the larger regional energy market, under an LMP-based congestion management system. The Parties to the West TOA (including PJM) further agree not to oppose formation of such an ITC. Allegheny further states that the Duquesne Light Company (Duquesne) may possibly join the PJM West RTO which will further improve the PJM system. We do not interpret the PJM West proposal to violate the open architecture requirements of Order No. 2000.

O. Rate Issues

1. Allegheny's Proposal

Upon joining PJM West, Allegheny states that it would recover its revenue requirement through the PJM OATT, principally through zone of delivery charges, *i.e.*, that the Allegheny system would become a transmission pricing zone within PJM, with individual zonal rates for delivery within its zone, similar to those used by PJM's current transmission-owning members. For transmission service "through" or "out" of the combined PJM West and PJM control areas, a single regional average rate would be charged. The license plate rate design applicable to PJM West would remain in effect through December 31, 2004. Allegheny proposes to establish its revenue requirement and zonal rates based on its currently effective OATT rates, which reflect a 1994 test period.³⁶

Allegheny states that it is proposing certain modifications to its existing OATT rates in order to achieve consistency with the rate design used in the PJM OATT. First, for point-to-point service with delivery taken within its zone, Allegheny proposes to change its existing point-to-point service rate of \$1.49/kW/month, which is based on an annual coincident-peak load (1 CP) divisor and test-year 1994 load data, to \$1.75/kW/month, based on a divisor reflecting the average of the twelve monthly

³⁵Id. 31,168.

³⁶Allegheny explains that its current rates are the result of a settlement approved in Docket No. ER96-58-000. See Allegheny Power Service Corporation, 85 FERC ¶ 61,275 (1998).

coincident-peak loads (12 CP) and test-year 1994 load data. Second, Allegheny proposes to change its network service charge, which currently reflects a rolling average 12 CP load ratio share allocation of its network revenue requirement, to a stated rate reflecting a 1 CP load divisor based on 1994 test-year load data. Third, Allegheny converts its existing rate for Schedule 2, Reactive Supply and Voltage Control from Generation Sources Service, into an annual revenue requirement by multiplying this rate by its calendar year 2000 billing determinants.³⁷ Allegheny states that use of such a revenue requirement under the PJM formula would result in total Schedule 2 charges for the Allegheny zone under the PJM OATT that are virtually the same as under the present Allegheny OATT. With regard to Schedule 1A, Transmission Owner Scheduling, System Control and Dispatch Service, of the PJM OATT, Allegheny states that it is not proposing a Schedule 1A charge in this filing, but that it may make a future rate proposal with respect to this particular ancillary service.

Allegheny states that it is also proposing a revised PJM region-wide rate for through or out service. This rate (recalculated to include Allegheny) would be \$1.765/kW per month, compared to the current rate of \$1.767/kW per month.

Allegheny states that if PJM West is integrated into PJM, as proposed, Allegheny would experience a \$24.5 million per year loss of transmission revenues due to Allegheny's termination of its existing through and out transmission service. In addition, Allegheny states that it would incur approximately \$10 million in start-up expenses associated with the formation of PJM West. Allegheny further states that retail rate caps and moratoria currently in place in its control area would prevent it from recovering these expenses and lost revenues from retail customers over the next several years. Allegheny states that were it required to absorb these costs, it could not voluntarily choose to join a PJM RTO. To address this concern, Allegheny proposes certain mechanisms to ensure that, for a transition period of four years, it remains revenue neutral as a result of joining PJM.

Allegheny proposes two transitional surcharges, a transitional market expansion charge (TMEC) and a transitional revenue neutrality charge (TRNC), to recover

³⁷Schedule 2, Reactive Supply and Voltage Control from Generation Sources Service, under the PJM OATT, contains a formula which allocates the generation owners' monthly revenue requirements among PJM OATT transmission customers, based on the same rate design used for the base transmission charge, *i.e.*, a license plate rate for delivery within a transmission pricing zone and a regional average rate for through or out service and current monthly network and point-to-point service billing determinants.

Allegheny's lost revenues and start-up costs.³⁸ The TMEC would consist of a uniform charge of \$0.007 for each megawatt hour of energy input into the combined PJM and PJM West transmission systems (either delivered from generation within the control areas or imported from outside of the control areas) and \$0.0381 for each megawatt hour of energy delivered from the combined PJM and PJM West transmission systems pursuant to PJM OATT transmission service (either delivered to load within the control areas or exported from the control areas). Allegheny states that the value of the TMEC is designed to reflect the benefits, to existing PJM entities, associated with the recovery of PJM's administrative costs, under Schedule 9 of the PJM OATT, from a wider base of market participants, *i.e.*, reflecting the addition of PJM West. The values of the proposed TMEC surcharges reflect PJM's estimation that generation providers (including importers) and load/exporters supply approximately 15 percent and 85 percent, respectively, of the revenues generated under Schedule 9 of the PJM OATT. Allegheny states that with calendar year 2000 billing determinants, and assuming Duquesne is a member of PJM West, the TMEC would recover approximately \$15 million annually, of which \$13.8 million would be allocated to Allegheny and \$1.2 million would be allocated to Duquesne.³⁹

Allegheny includes estimates of savings under Schedule 9 of the PJM OATT, provided to it by PJM, assuming, under one scenario, that both Allegheny and Duquesne join PJM; and under another scenario that only Allegheny joins PJM. Under the former scenario, PJM estimates annual savings of \$15.2 million, \$19.6 million, and \$20.8 million, in calendar years 2002, 2003, and 2004, respectively, while under the latter scenario, PJM estimates annual savings of \$11.4 million, \$15.0 million, and \$16.1 million. Allegheny notes that assuming both Allegheny and Duquesne join PJM, the TMEC revenues would represent virtually all of the first year administrative charge savings estimated by PJM, but only about 75 percent of the second and third year savings. Thus, under this scenario, after the first year, existing PJM entities would experience net Schedule 9 charge savings from the expansion of PJM.

³⁸ Allegheny claims that these lost revenues and start up costs will total \$27.7 million, per year, over a four year period, reflecting lost revenues of \$24.5 million per year, plus \$3.2 million per year associated with a four-year amortization of its \$10 million in start-up costs and a 10.5 percent annual cost of money.

³⁹ Allegheny states that the TMEC revenues would likely be less if Duquesne does not join, but reports that PJM has not provided an estimate of TMEC revenues under that scenario.

In addition, the TRNC would consist of an adder to the rates for through or out service. The proposed value of the TRNC would be \$0.30/kW per month for firm service, and \$0.24/kW per month and \$0.00033/kWh for non-firm service. Allegheny estimates that the TRNC would recover about \$13.6 million annually.

Allegheny also proposes true-up and sunset mechanisms covering both of its proposed surcharges. Specifically, the TMEC and TRNC surcharges would remain in effect until they produce cumulative revenues of \$110.8 million for Allegheny (reflecting projected annual revenues of \$27.7 million recovered over a four-year period).

Allegheny states that its proposed surcharge term (extending through 2005), would coincide with the average period during which retail rate caps will remain in place within Allegheny's service territory. Should Duquesne join PJM West, Allegheny states that it would not adjust the value of the proposed TMEC or TRNC. Rather, a portion of the TMEC and TRNC revenues would be allocated to Duquesne based on its annual lost revenues, with the cumulative revenue target adjusted upward to include Duquesne's lost revenues.

Allegheny states that its proposed surcharges are consistent with the Commission's policy of preserving revenue neutrality for transmission owners seeking to create RTOs.⁴⁰ In this regard, Allegheny notes that the TRNC, when added to the base rate, results in a rate for through or out service of \$2.065/kW/month, which is less than the zonal delivery rate for one PJM pricing zone, and only slightly more than the zonal delivery rate for two other PJM pricing zones. Allegheny submits that the resulting through or out service rate, including the TRNC, would not result in any disparity between the rate for through or out service, and the rates for internal delivery. Finally, Allegheny states that most customers would pay lower rates for transmission during the transition period and that the proposed through and out charge has the added benefit of being a uniform rate.

2. Responsive Pleadings

Several intervenors object to Allegheny's proposal to use a test-year 1994 revenue requirement and 1994 load data to calculate Allegheny's proposed point-to-point and network service rates. American Municipal Power-Ohio, Inc. (AMP-Ohio) and Harrison Rural Electrification Association (Harrison) contend that Allegheny has not justified its

⁴⁰See Allegheny's transmittal letter at p. 18, citing Alliance III and Order No. 2000 at 31,172.

proposed surcharges or taken into consideration all of the offsetting cost savings that could have the effect of lowering these surcharges (cost factors such as the additional accumulations of depreciation in excess of additional transmission investment, increases in short-term transmission revenues, or cost-reductions associated with the transfer of responsibilities from Allegheny to the PJM RTO).

Chambersburg argues that Allegheny may have experienced load growth since 1994 and that use of 1994 load data would be inconsistent with Allegheny's proposed use of 2000 load data to calculate its rate for Reactive Supply and Voltage Control from Generation Sources Service. Chambersburg submits that a current load figure should be used to calculate Allegheny's zonal network rate.

Other intervenors argue that even without Allegheny's proposed transitional surcharges, Allegheny's proposed rates would produce an unjustified windfall. AEC, et al. argue that this windfall would be achieved, with respect to Allegheny's proposed point-to-point service rates, due to the conversion from a 1-CP demand divisor to a 12-CP demand divisor. With respect to Allegheny's proposed network service charges, this windfall would be achieved by the switch from the rolling 12-month average load ratio share allocation in Allegheny's current OATT to a stated rate based on a 1994 1 CP load divisor. AEC, et al. urge the Commission to require Allegheny to use calendar-year 2000 billing determinants for the network rate divisor in order to achieve true revenue neutrality.

Chambersburg notes that Allegheny's rate proposal fails to include any information regarding potential charges under Schedule 1A, Transmission Owner Scheduling, System Control and Dispatch Service, of the PJM OATT. Chambersburg argues that before Applicants are permitted to recover any charges under Schedule 1A, Applicants should be required to make a section 205 filing. Chambersburg also takes issue with Allegheny's proposed use of its calendar year 2000 load data for purposes of calculating its proposed Schedule 2 charges. Chambersburg argues that this load data is overstated because it fails to net out all of Allegheny's pre-Order No. 888 transactions.

A number of intervenors also take issue with Allegheny's proposed transition surcharges. Most of these intervenors argue that Allegheny's claimed lost revenues and start-up costs have not been supported. Chambersburg states that aside from the \$100,000 amount used mainly for communications equipment, Allegheny's estimated start-up expenses of \$10 million have not been supported. It requests that Allegheny be required to make a separate filing, under section 205 of the FPA, after these costs become final, in order to recover them.

Delaware Municipal Electric Corporation, Inc. (DEMEC) requests that the Commission consider requiring that congestion charge revenues be used to reduce alleged revenue shortfalls. Chambersburg submits that Allegheny may experience cost savings from transferring operation, maintenance, and planning responsibilities to PJM. Chambersburg requests that the Commission require Allegheny to provide information on anticipated savings, and to use any related savings to mitigate the impact of its revenue losses.

Strategic and Municipalities ⁴¹ recommend that any increase in network service revenues, resulting from the switch from the rolling 12 CP load ratio share allocation to a fixed 1994 1 CP network rate divisor, be credited against Allegheny's transition costs. AEC, et al. maintain that start-up costs are an added cost-of-service item that should not be treated incrementally; *i.e.*, such costs should be considered within the context of a full rate case. AEC, et al. argues that Allegheny's entitlement to recover transitional surcharges should be tied to its filing of a cost-of-service study demonstrating that Allegheny's proposed rates and retail rates would in fact produce the revenue shortfall claimed by Allegheny.

Intervenors also protest the allocation of these costs. The Virginia Commission, for example, notes that while through and out transactions would be charged both the TMEC and TRNC, internal deliveries would be assessed only the TMEC. Duke complains that Allegheny's proposed transition costs will be recovered disproportionately from wholesale customers who take through and out transmission service, and argues that, instead, the costs should be recovered from transactions that will benefit from the RTO formation.

AEC, et al. argue that Allegheny's proposal to recover transition costs indiscriminately charges customers regardless of benefit. They further maintain that the appropriate place to recover the transition costs is on transactions coming across the existing Allegheny/PJM boundary, as it is the parties to such transactions that will receive the benefits of PJM West. Similarly, Strategic contends that Allegheny has not justified charging the TMEC to those loads and generators in PJM that do not benefit from the elimination of pancaking. AEC, et al. and GPU note that the TMEC is based on an estimation of benefits that assumes that Duquesne joins PJM West. Thus, if Duquesne does not join, the TMEC may exceed even claimed benefits.

⁴¹Municipalities comprise the City of Hagerstown, Maryland, the Town of Thurmont, Maryland, the Town of Williamsport, Maryland, and the Town of Front Royal, Virginia.

PPL and GPU object to Allegheny's proposal to charge other PJM transmission owners for start-up costs, including those proposed to be capitalized by PJM. PPL and GPU argue that these transmission owners have already incurred their share of PJM's start-up costs. GPU argues that it is unduly discriminatory for one member of an expanded PJM to recover its share of start-up costs from the other members, as existing members were not afforded similar opportunity to shift their expenses to a region-wide charge.

GPU submits that RTO formation could be discouraged if original members are discriminated against and subject to increased costs due to new membership. PPL asserts that start-up costs associated with PJM West and Allegheny's Order No. 2000 compliance are likely to be much less than Allegheny would incur if it joined a totally new RTO. PPL requests that the TMEC revenues be capped at \$13.8 million annually, with a December 31, 2004 end date. PPL asserts that Allegheny should have an opportunity to recover transition costs ending at a date certain, with no guaranteed cumulative amount.

3. Discussion

We will conditionally approve Allegheny's proposal to use a license plate rate design applicable to PJM West, through December 31, 2004. In Order No. 2000, we stated that where we approve the use of license plate rates for an initial fixed term, we will require that, prior to the end of the fixed term, the RTO must complete an evaluation of the design of its rates for fixed cost recovery based on its specific circumstances and file with the Commission its recommendations on any changes that should be instituted.⁴² Accordingly, we will require PJM RTO to perform such an evaluation and file its recommendations with the Commission at least 60 days prior to January 1, 2005. In that filing, PJM RTO should provide justification for its recommendation to continue or discontinue the use of license plate rates, or otherwise change the method for fixed cost recovery under the PJM OATT.⁴³

Consistent with our rulings addressing the Alliance RTO, we will also approve Allegheny's proposed use of the revenue requirement reflected in its currently-effective

⁴²Order No. 2000 at 31,177.

⁴³Id.

OATT for calculating its point-to-point and network service rates.⁴⁴ Requiring Allegheny to revise its rates to reflect an updated cost-of-service study would be inconsistent with the revenue neutrality concept, discussed below. As such, we will not require Allegheny to provide an updated cost of service study.

With regard to Allegheny's proposal to develop its zonal point-to-point rate based on a 12 CP divisor and to fix its network service rate based on a 1 CP divisor, we find that Allegheny's proposal is inconsistent with our prior determinations applicable to the PJM OATT. First, PJM's unit charges for both point-to-point and network service are based on the average of the 12 monthly peaks.⁴⁵ In our order approving that methodology, we also found that the billing determinants for the network service charge should reflect the network customers' annual coincident peak loads, consistent with the assignment of FTRs to network service customers in amounts equal to their annual coincident peak load.⁴⁶ We further found that this change would require a corresponding change to the divisor used to develop the unit charge.⁴⁷

This methodology was a limited modification to the 12 CP divisor originally proposed by the supporting transmission owners for the unit charge applicable to network service, not an adoption of a 1 CP divisor for network service. Moreover, Allegheny's proposed rate divisors reflect coincident-peak loads, with no apparent adjustment to reflect firm point-to-point contract demand reservations, as required by Order No. 888.⁴⁸ Therefore, we will require Allegheny to revise its proposed rates for

⁴⁴See Alliance IV at n. 59.

⁴⁵See 81 FERC at 62,250.

⁴⁶Id. at 62,261.

⁴⁷As noted earlier, the divisor will reflect the average of 12 monthly peaks rather than the annual peak. However, the network service "peaks" will reflect the monthly FTR MW rather than the actual network monthly load MW. Id. at n. 127.

⁴⁸See Order No. 888, Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Access Utilities and Transmitting Utilities, FERC Statutes and Regulations, Regulation Preambles January 1991-June 1996 ¶ 31,036 at 31, 738 (1996) (Order No. 888), order on reh'g. Order No. 888-A, FERC Stats. & Regs. ¶ 31,048 (1997), order on reh'g. Order No. 888-B, 81 FERC ¶ 61,248 (1997), order on reh'g. Order No.

(continued...)

both network and point-to-point services) to reflect a 12 CP divisor, with the monthly network service peaks reflecting the monthly FTR MW, rather than monthly coincident-peak network loads. In addition, Allegheny should subtract the monthly coincident peak demands associated with all firm point-to-point service customers and add the monthly contract demand reservations for all firm point-to-point service.

As modified above, we will approve Allegheny's proposal to use 1994 data to develop its stated network service charge. However, to the extent that Allegheny has experienced an increase in network load and firm point-to-point reservations since the 1994 test year, use of 1994 test-year demand data would increase the per-unit network service charges and revenues above those levels achieved with the rolling load ratio share allocation currently reflected in the Allegheny OATT. In its answer, Allegheny states that it did not intend to effect either a rate increase or rate decrease for its existing wholesale network customers, and that it has been in contact with one customer group in an effort to resolve this issue. We see no reason why, in conjunction with being held harmless from lost revenues, Allegheny should not similarly hold all existing network customers harmless from the conversion to a 1994 test-year rate denominator. Therefore, we will direct Allegheny to propose, in a compliance filing, a mechanism to hold existing network customers harmless in making the conversion Allegheny proposes. We urge Allegheny to confer with all affected customers in preparation of that filing in an effort to arrive at a satisfactory mechanism.

With respect to Allegheny's charges under Schedule 1A, Transmission Owner Scheduling, System Control and Dispatch Service, Allegheny states that it is not proposing a charge in this filing, but may make a rate proposal for this service in the future. We remind Allegheny and PJM that any charges under Schedule 1A that are not in strict conformance with that schedule will constitute a change in rates subject to the filing requirements of section 205.

With regard to Allegheny's proposed revenue requirement for Schedule 2, Reactive Supply and Voltage Control from Generation Sources Service, we agree with intervenors that billing determinants associated with all pre-Order No. 888 contracts should be netted out for the purpose of deriving Allegheny's revenue requirement. That

⁴⁸(...continued)

888-C, 82 FERC ¶ 61,046 (1998), aff'd in relevant part sub nom. Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir 2000), cert granted, 69 U.S.L.W. 3574 (Nos.00-568 (in part) and 00-809) cert. Denied., id. (No. 00-800) (U.S. Feb. 26, 2001).

revenue requirement will be allocated only among PJM OATT customers, and will, therefore, be fully recovered from PJM OATT customers. Therefore, including pre-Order No. 888 contract billing determinants in the derivation of that revenue requirement would result in total Schedule 2 charges for the Allegheny zone under the PJM OATT in excess of revenues under the present Allegheny OATT. This result would be contrary to Allegheny's representation of its proposal,⁴⁹ and inconsistent with the revenue neutrality concept, discussed below. In its compliance filing, Allegheny should include a revised revenue requirement for reactive power service, excluding all pre-Order No. 888 contract billing determinants and provide supporting information.

Consistent with our rulings addressing the Alliance RTO,⁵⁰ we will provisionally approve Allegheny's entitlement to recover lost revenues associated with its membership in the PJM RTO through transitional surcharges, and the proposed design of these surcharges. Beyond this conceptual entitlement to recover these surcharges, however, Allegheny has not demonstrated the reasonableness of the specific surcharges it proposes. Specifically, Allegheny has failed to support the costs it claims it will incur in connection with its joining the PJM RTO, and has failed to support the derivation of its proposed surcharges.

Allegheny proposes to establish the value of the TMEC to mirror the benefits that existing PJM entities will receive as a result of the formation of PJM West. This is consistent with the approach taken by Alliance RTO in its design of its zonal transmission adjustment (ZTA), which we approved in Alliance III,⁵¹ and we find it reasonable here as well. In addition, we find that the magnitude of the resulting through and out rate, including the TRNC, is not out of line with the zone of delivery charges in PJM. Therefore, we disagree with intervenors' arguments that the proposed surcharges

⁴⁹See Allegheny's transmittal letter at 16 and Exh. JFB-1, prepared testimony of Joseph F. Baier at 10.

⁵⁰See Alliance I at 61,922 and 61,929 and Alliance III at 61,311.

⁵¹The ZTA is a uniform surcharge for deliveries within the Alliance regional transmission system. It is calculated separately for each transmission pricing zone, and reflects the historical transmission charges that the Alliance transmission owner in a particular zone has paid to other Alliance transmission owners to serve load within its own zone. Thus, the ZTA is designed to collect additional revenue from each zone in proportion to the benefits that the particular Alliance transmission owner will realize when it no longer has to pay pancaked rates for transmission purchased from another Alliance company to serve load within its zone. See Alliance III at 61,309 and 61,311.

fall disproportionately on through and out service. In addition, we reject suggestions that the appropriate place to recover all of the transition costs is on transactions coming across the existing Allegheny/PJM boundary. This proposal would essentially restore pancaked rates, and, thus, violate one of the fundamental tenets of Order No. 2000.

Intervenors raise numerous concerns regarding Allegheny's quantification of its lost revenues and start-up costs. We generally share these concerns. For instance, it is not clear whether all pre-Order No. 888 contract revenues have been excluded from the lost revenue amount. It is also unclear whether all point-to-point service revenues associated with delivery within the Allegheny control area have been excluded from the revenue loss estimate, even though Allegheny will receive the full revenues associated with such transactions under the license plate rate design. Similarly, it is unclear if any ancillary service revenues are included in the lost revenues, and whether those revenues are appropriately considered lost as a result of Allegheny's joining PJM West. In addition, while Allegheny properly nets against its lost revenues its expected share of revenues associated with regional through and out service, it has provided no back-up support for the value of those expected revenues. In its compliance filing, Allegheny should provide detailed support for its estimated lost revenues addressing the above concerns. Such support should include all source data and calculations performed on that source data, as well as full documentation and explanation of such data and calculations, including all assumptions and the basis for those assumptions.

Intervenors also raise concerns regarding the value of the proposed surcharges, and we share these concerns as well. Allegheny has failed to support the benefits to existing PJM market participants associated with expanding the recovery of PJM's administrative costs to transactions involving the PJM West region. It has also failed to support the derivation of its unit charges and the projected revenues from the transitional surcharges. In its compliance filing, Allegheny should provide detailed support for the projected benefits concerning PJM administrative costs, taking into consideration any countervailing effect of increases in PJM's administrative costs due to the implementation of PJM West, including, but not limited to, capitalizable expenses associated with the start-up of PJM West. It should also provide detailed support for the derivation of its unit charges and projected revenues. Such support should include all source data and calculations performed on that source data, as well as full documentation and explanation of such data and calculations, including all assumptions and the basis for those assumptions.

In addition, several intervenors argue that Allegheny has failed to quantify and credit against its claimed lost revenues and start-up costs: (i) expected cost savings from transferring operation, maintenance, and planning responsibilities to PJM; (ii) increased

network service revenues resulting from the switch from the rolling load ratio share allocation to a fixed 1994 network rate divisor; or (iii) revenues Allegheny will receive from the distribution of congestion credits in excess of those due FTR holders or from the sale of FTRs. We direct Allegheny to address these concerns in its compliance filing. It should also identify and quantify any savings or additional revenue sources associated with its joining PJM West and provide full support for such analysis consistent with the instructions outlined above.

We agree with AEC, et al. and GPU that because the TMEC is based on an estimation of benefits that assumes that Duquesne joins PJM West, if Duquesne does not join, the TMEC may exceed benefits. As to Allegheny's proposal to not adjust the value of the proposed TMEC or TRNC should Duquesne join PJM West, we find it premature and speculative as to the conditions under which Duquesne will seek to join PJM, if it, indeed, seeks to join PJM at all. In its compliance filing, Allegheny should calculate its TMEC and TRNC surcharges assuming that only Allegheny joins PJM. In the event that Duquesne joins PJM West in the future, an appropriate filing may be made at that time to seek adjustments to the transition surcharges to reflect additional transition costs or benefits.

In addition, we agree with GPU that it is inappropriate to require existing PJM members to share in the start-up costs incurred by Allegheny in joining PJM. Allegheny is therefore directed to eliminate the inclusion of start-up costs from surcharges applicable to existing PJM entities.

Finally, with regard to the appropriate period for quantification and recovery of lost revenues, we find that the quantification of lost revenues and the recovery of those revenues should be consistent with the effectiveness of the proposed license plate rate design, *i.e.*, through December 31, 2004. While we are not necessarily opposed to the originally proposed period (through December 31, 2005) for both quantification and recovery of lost revenues, we find that it is premature to quantify lost revenues for 2005 when the rate for that year is yet to be determined. Allegheny may file to recover any lost revenues associated with 2005 when an accurate quantification is possible, and we will address their filing at that time.

The Commission orders:

(A) Applicants' RTO compliance filing is hereby provisionally accepted, subject to the conditions discussed in this order, and subject to the PJM RTO Order.

(B) Allegheny is hereby directed to make a compliance filing on all rate issues discussed in the body of this order, within 60 days of the date of this order.

(C) Applicants are hereby directed to make a compliance filing within 60 days of the date of this order addressing all matters as discussed in the body of this order.

By the Commission. Commissioner Massey concurred with a separate statement attached.

(S E A L) Commissioners Breathitt and Wood dissented in part with separate statements attached.

David P. Boergers,
Secretary.

Appendix

RT01-98-000
PJM Interconnection, L.L.C. and the Allegheny Power
System: Monongahela Power Company, The Potomac Edison
Company, and West Penn Power Company

Intervenors

AES NewEnergy Inc.
Allegheny Electric Cooperative, Inc. and Old Dominion Electric Cooperative*
American Forest & Paper Association
American Municipal Power-Ohio, Inc.*
Borough of Chambersburg, Pennsylvania*
Cities and Towns of Hagerstown, Thurmont, and Williamsport, Maryland, and the Town
of Front Royal, Virginia*
Commonwealth Edison Company, Exelon Generation Company LLC , and PECO
Energy Company
Conectiv
Delaware Municipal Electric Corporation, Inc.*
Duke Energy North America, LLC*
Duquesne Light Company
Dynegy Power Marketing, Inc.
Edison Mission Energy
Enron Power Marketing, Inc.
FirstEnergy Corp.*
GPU Energy*
Harrison Rural Electrification Association*
KeySpan-Ravenswood, Inc.
Maryland Office of People's Counsel*
Maryland Public Service Commission
Mid-Atlantic Power Supply Association*
Midwest Independent Transmission System Operator, Inc.
Mirant Chalk Point, LLC, Mirant Mid-Atlantic, LLC, Mirant Peaker, LLC, and Mirant
Potomac River, LLC*
Morgan Stanley Capital Group Inc.
Norton Energy Storage L.L.C.

Orion Power Midwest, L.P.*
Pennsylvania Office of Consumer Advocate*
PJM Industrial Customer Coalition
PPL Electric Utilities Corporation and PPL EnergyPlus, LLC
Public Utilities Commission of Ohio
Reliant Energy Northeast Generation, Inc.*
Shell Energy Services Company, L.L.C.
Strategic Energy L.L.C.*
Virginia State Corporation Commission*
Williams Energy Marketing & Trading Company

* parties filing protests or comments

RT01-10-000
Allegheny Power

Intervenors

American Wind Energy Association and Project for Sustainable FERC Energy Policy*
Borough of Chambersburg, Pennsylvania*
Calpine Eastern*
Cities and Towns of Hagerstown, Thurmont, and Williamsport, Maryland, and the Town
of Front Royal, Virginia*
Coalition of Midwest Transmission Customers and PJM Industrial Customer
Coalition*
Coastal Merchant Energy, L.P.
Constellation Power Source, Inc.
Delaware Municipal Electric Corporation, Inc.*
Dynegy Inc.*
Edison Mission Energy and Edison Mission Marketing & Trading, Inc.
Electric Power Supply Association*
Enron Power Marketing, Inc.
Joint Consumer Advocates*
Maryland Public Service Commission*
Midwest Independent Transmission System Operator, Inc.
Morgan Stanley Capital Group Inc.*

National Rural Electric Cooperative Association
Norton Energy Storage LLC
Pennsylvania Public Utility Commission
PG&E National Energy Group
PJM Interconnection, L.L.C.*
PPL Electric Utilities Corporation and PPL EnergyPlus, LLC*
Public Utilities Commission of Ohio*
Shell Energy Services Company, L.L.C.*
Tenaska, Inc.
Southern Energy Chalk Point, LLC; Southern Energy Mid-Atlantic, LLC;
Southern Energy Peaker, LLC, and Southern Energy Potomac River, LLC
The Williams Companies*

* parties filing protests or comments

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

PJM Interconnection, L.L.C. and
Allegheny Power

Docket No. RT01-98-000

Allegheny Power

Docket No. RT01-10-000

(Issued July 12, 2001)

MASSEY, Commissioner, concurring:

In this order, the Commission expresses its intention to evaluate in the near future the importance of standardizing generation interconnection procedures. I've long advocated such standardization, so this is a big step in the right direction. But I would have been clearer and firmer in expressing our resolve to standardize interconnection procedures. For me, the time to evaluate whether to do so is past. It's time simply to do it.

Interconnection standardization is good for the market. Generators should make location decisions based on economics, not on the basis of a patchwork of idiosyncratic interconnection standards. Establishing uniform standards will be good for generation investment and good for consumers. And standardization would be an efficient use of the Commission's staff resources. It's no secret that the staff is laboring under a crushing work load. Processing a multitude of interconnection filings eats up staff time. Standardization will free staff for other important work.

Therefore, I concur with today's order.

William L. Massey
Commissioner

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(Issued July 12, 2001)

Breathitt, Commissioner, dissenting, in part:

Since the Commission began promoting RTOs as a means to remove barriers and impediments to wholesale electricity markets, I have been fully committed to the goal of implementing RTOs. However, I am dissenting, in part, to express my objections to specific language in this order and other RTO orders on today's agenda supporting the creation of four RTOs in the country. I agree with the majority's claim that the Commission has been attempting to facilitate the development of large RTOs reflecting natural markets since we issued Order No. 2000. That was our stated goal and one that I have actively pursued. However, today's orders go further by stating that the Commission "favors the development of one RTO for the Northeast, one RTO for the Midwest, one RTO for the Southeast, and one RTO for the West." I do not necessarily favor such development.

When the Commission deliberated over how to attain our mutual objective of RTO formation, we decided to adopt an open collaborative process that relied on voluntary regional participation. The intent was to design RTOs so that they could be tailored to the specific needs of each region. We specifically declined to propose fixed or specific regional boundaries under section 202(a) of the FPA. Instead, we concluded, as a matter of policy, that we would not attempt to draw boundaries, based upon our conviction that transmission owners, market participants, and regulators in a particular region have a better understanding of the dynamics of the transmission system in that region, and that they should propose the appropriate scope and regional configuration of an RTO. We did not specifically endorse one particular scheme of RTO configuration, but opted instead to establish appropriate guidelines to aid in RTO development. In fact, our regulation requires only that an appropriate region is one of sufficient scope and configuration to permit an RTO to maintain reliability, effectively perform its required functions, and support efficient and non-discriminatory power markets.

Today's order represents a dramatic departure from the approach we pursued in Order No. 2000 to the extent that it directs the formation of four specific RTOs. Just as some commenters to our RTO rulemaking feared, the Magic Markers have come out, and

the boundaries are being drawn with little regard to the status and timing of RTO formation efforts in various regions of the country. This was not my intent at the time we issued Order No. 2000; and the events since we issued Order No. 2000 do not compel me to embrace this policy shift. Parties have spent many hours and countless resources in negotiations, collaborations, and complicated business strategy sessions to develop reasonable RTO approaches. The impact of the majority's directive that these four RTOs be formed could be to render these efforts useless and force parties to begin the difficult and time-consuming process anew. For example, the Midwest ISO -Alliance settlement, which the Commission approved and which represented a tremendous effort by many parties, could unravel.

If the majority believes that the Commission should depart from the basic philosophies embodied in Order No. 2000, then I believe it would be only appropriate to initiate a formal notice-and-comment rulemaking proceeding so that we could make a reasoned decision informed by the views of the stakeholders in this process – state commissions, chief among others.

Finally, I do not adopt the majority's assertion that forming larger RTOs will result in lower wholesale electricity prices. This is a laudable goal, and as such, I embrace it. As a general proposition, Order No. 2000 encouraged the development of large RTOs. However, the promise of lower wholesale electricity prices is one that I, as a federal official, am not willing to make to consumers at this time.

For these reasons, I respectfully dissent.

Linda K. Breathitt
Commissioner

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PJM Interconnection, L.L.C. and
Allegheny Power

Docket No. RT01-98-001

Allegheny Power

Docket No. RT01-10-000

(Issued July 12, 2001)

Wood, Commissioner, dissenting in part:

I support this order and write separately only to dissent on the length of the transition from license plate to RTO-wide rates in PJM West. In this case, no showing was made that deferral of implementation of full RTO-wide rates was necessary. The negative impact which continuation of license plate rates has on smooth and swift development of competitive power markets should be balanced against retail customer bill impacts. For example, suppose a typical homeowner with a \$120/month electric bill gets a ten percent increase in transmission rates. She would see a 72-cent increase in her monthly bill as a result. I do not consider such small shifts up or down to be material enough to warrant delay in moving to uniform RTO-wide transmission rates. As a guideline, I would think that total retail customer bill shifts greater than 3 percent may warrant use of a transitional device such as continuation of license plate rates, but any shift smaller than that would not.

An RTO transmission rate should, of course, fully compensate all transmission service providers whose costs are being recovered in that rate for their full revenue requirement amounts.

On an additional matter, I am concerned about the use of a 7 year old cost study to establish rates. Creation of an RTO is a good time to start anew with a fresh look at cost levels, allocations and rate designs. It should be done here.

Respectfully submitted,

Pat Wood, III
Commissioner