

UNITED STATES OF AMERICA 101 FERC ¶ 61,033
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, Linda Breathitt,
And Nora Mead Brownell.

Arizona Public Service Company
El Paso Electric Company
Public Service Company of New Mexico
Tucson Electric Power Company

Docket No. RT02-1-000

WestConnect RTO, LLC

Docket No. EL02-9-000

DECLARATORY ORDER ON REGIONAL
TRANSMISSION ORGANIZATION

(Issued October 10, 2002)

1. On October 15, 2001, Arizona Public Service Company (APS), El Paso Electric Company (EPE), Public Service Company of New Mexico (PNM), and Tucson Electric Power Company (TEP) (collectively, Applicants)¹ filed a petition for declaratory order that seeks the Commission's guidance on whether their proposal to form a regional transmission organization (RTO), WestConnect RTO, LLC (WestConnect), satisfies the Commission's requirements for an RTO under Order No. 2000.²

¹Applicants include only the Commission-jurisdictional public utilities that have participated in the development of WestConnect. In addition, Applicants note that the Salt River Project Agricultural Improvement and Power District (Salt River), the Western Area Power Administration (Western), and the Southwest Transmission Cooperative, Inc. (Southwest Transmission) (collectively, Non-Jurisdictional Entities) also participated in WestConnect's development.

²See *Regional Transmission Organizations*, FERC Stats. & Regs. ¶ 31,089 at 30,993 (1999), 65 Fed. Reg. 810 (2000) (Order 2000), *on reh'g*, Order No. 2000-A, FERC Stats. & Regs. ¶ 30,092, 65 Fed. Reg. 12,088 (2000), *aff'd*, *Public Utility District No. 1 v. FERC*, 272 F.3d 607 (D.C. Cir 2001).

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2. For the reasons discussed below, we find that certain aspects of Applicants' proposal satisfy the Commission's requirements for an RTO under Order No. 2000.³ In addition, we provide guidance on how the Applicants' proposal, if modified to address various issues, could meet the requirements of Order No. 2000 (thereby qualifying for RTO status) and could provide the basic framework for a standard market design for the Southwest.

3. With the issuance of this order concerning Applicants' proposal, the Commission has provided guidance on the three principal RTO proposals in the Western Interconnection: CAISO, RTO West, and WestConnect.⁴ To achieve the efficiencies reflected in those market design proposals, we believe that it is imperative that the proponents of these organizations, Western market participants, and other interested parties all work cooperatively to identify common commercial practices among the proposals as well as potential market design elements that could create seams between the organizations. Where potential seams issues are identified, we direct CAISO, RTO West, and WestConnect and strongly encourage market participants and other interested parties to collaborate through the Seams Steering Group - Western Interconnection (Steering Group) on solutions to such issues, thus ensuring that markets in the West can achieve their fullest potential benefit.

4. Because there is a broad overlap of issues in the proposal before us and in the Commission's recently issued notice of proposed rulemaking on Standard Market Design,⁵ the Commission has reviewed Applicants' proposal in light of the principles and proposed requirements contained in the Standard Market Design NOPR. As we recently stated with regard to other pending RTO proposals, we look at this filing as both

³See id.

⁴See California Independent System Operation Corporation, 100 FERC ¶ 61,060 (2002); Avista Corporation, et al., 100 FERC ¶ 61,274 (2002).

⁵See Remedying Undue Discrimination Through Open Access Transmission and Standard Electricity Market Design, Notice of Proposed Rulemaking, 67 Fed. Reg. 55, 452 (Aug. 29, 2002), FERC Stats. & Regs. ¶ 32,563 (2002) (Standard Market Design NOPR).

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informing, and being informed by, the Standard Market Design NOPR.⁶ Our review of Applicants' proposal therefore not only approves or conditionally approves various elements of the proposal, but also provides guidance in areas which we do not find consistent with the basic principles of the Standard Market Design NOPR. Further, because of the extensive efforts committed by industry participants to developing a framework for a sound RTO proposal here, we take this opportunity to clarify that it is not this Commission's intent to overturn, in the final Standard Market Design rule, decisions that are made in this docket. In other words, unless the Commission has specifically indicated in this order that an element of the RTO proposal is inconsistent with the Standard Market Design proposal or needs further work in light of the Standard Market Design proposal, we do not intend, in the final Standard Market Design rule, to revisit prior approvals or acceptances of RTO provisions because of possible inconsistencies with the details of the final rule. This Commission intends to take all appropriate steps at the final rule stage of the Standard Market Design rulemaking to ensure that, to the extent we have already approved or conditionally approved RTO elements, these approvals remain intact.

5. This order benefits customers because a properly formed RTO in the Southwest will promote the reliability of the Southwest electric grid and enhance competition.

6. Among other things, this order:

- approves, subject to certain modifications, Applicants' proposed governance structure and finds that WestConnect will be independent of market participants;
- approves Applicants' proposal to retain license plate rates for an interim period;
- approves the use of a grid charge to recover the costs of WestConnect's operations;
- approves, with modification, the proposed interconnection process;

⁶See Avista Corp., et al., 100 FERC ¶ 61,274 at P 3 (2002) (RTO West).

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- approves Applicants' proposal for the voluntary conversion of existing contracts;
- approves Applicants' procedures for addressing parallel path flow issues within their region;
- approves Applicants' market approach for providing ancillary services;
- approves, with modification, Applicants' proposal for planning and expansion;
- approves Applicants' market monitoring proposal;
- approves Applicants' congestion management proposal as a "Day One" mechanism and directs Applicants to engage in further discussions to develop a congestion management program that reflects market-driven solutions to clear congestion;
- finds Applicants' proposal for maintaining short-term reliability meets the requirements of Order No. 2000;
- finds acceptable Applicants' proposal for developing an RTO that includes all public utilities located in the Southwest and allows for participation by non-public utility entities in that area;

I. Background

A. Overview of Applicants' Filing

13. Applicants state that their filing evolved from an earlier Southwestern RTO project named DesertSTAR, Inc. (DesertSTAR) that envisioned a not-for-profit independent system operator and is, in large part, built upon that stakeholder process. Thus, this filing is the culmination of almost five years of effort to form an RTO for the southwestern United States.

14. Applicants note that this filing differs from the not-for-profit DesertSTAR model, because, among other things, WestConnect will operate as a for-profit entity. WestConnect will have the flexibility to become, upon acquiring existing transmission

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assets or building transmission assets of its own, a transco (i.e., it will own and invest in transmission facilities with the intention of earning a profit).

15. Applicants state that their application satisfies the requirements of Order No. 2000 and that it is a comprehensive RTO proposal that includes draft corporate formation documents, pro forma agreements, and a proposed tariff. Specifically, this filing includes: a draft Limited Liability Company Agreement of WestConnect (WestConnect LLC Agreement), which details the ownership structure, management requirements, and fiduciary responsibilities of WestConnect; a pro forma Transmission Control Agreement (WestConnect TCA), which details the operating duties among WestConnect and participating transmission owners (PTOs); the WestConnect Generator Agreement; and a WestConnect Scheduling Coordinator Agreement for federal and non-federal entities.

16. Applicants also filed an Open Access Transmission Tariff (WestConnect Tariff) that contains the rate formulas, terms, and conditions under which WestConnect will provide non-discriminatory transmission service over the facilities under its authority.⁷ The WestConnect Tariff also specifies the market rules for a restructured wholesale electric marketplace in the Southwest, including a market-based congestion management proposal.

17. Applicants state that this filing will be followed by the following: (1) filings under section 205 of the Federal Power Act (FPA)⁸ that will seek the Commission's acceptance of the actual WestConnect rates; and (2) filings that will seek approval, pursuant to section 203 and/or 205 of the FPA,⁹ for the transfer of control of their jurisdictional facilities to an RTO. Applicants state that they will also seek any necessary state commission or other governing authority approvals for a transfer of those assets.

⁷The WestConnect Tariff addresses, among other things: congestion management; scheduling; dispatch and emergency operations; ancillary services; treatment of existing contracts; outage coordination; market monitoring; a website that includes OASIS functions; transmission pricing; planning and expansion; generator interconnections; application provisions for PTOs and scheduling coordinators; and a proposed WestConnect code of conduct.

⁸See 16 U.S.C. § 824d (2000).

⁹See id. at § 824b and § 824d.

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B. Notices and Responsive Pleadings

18. Notice of Applicants' filing was published in the Federal Register, 66 Fed. Reg. 54,987 (2001), with comments, protests, and interventions due on or before November 15, 2001. Motions to intervene were filed by the parties listed in Appendix A of this order. Protests and comments were filed by the parties noted below in the discussion section of this order and as noted in Appendix B of this order. On December 17, 2001, Applicants filed an answer to the protests. In addition, on July 3, 2002, Applicants filed a supplement to their answer, and, on September 13, 2002, Applicants filed another supplement to their answer.

II. Discussion

A. Procedural Matters

19. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,¹⁰ the timely, unopposed motions to intervene and notices of intervention serve to make those who filed them parties to this proceeding. At this early stage of the proceeding, given the lack of undue prejudice or delay and given the party's interest, we find good cause to grant IDACORP Energy L.P.'s unopposed, untimely motion to intervene in this proceeding. Notwithstanding Rule 213 of the Commission's Rules of Practice and Procedure,¹¹ we accept Applicants' answer and the supplements to their answer, because they assist us in understanding the issues in this proceeding.

B. RTO Characteristic No. 1: Independence

The RTO must be independent from market participants.

1. Applicants' Proposal: Ownership Structure

20. Applicants propose that WestConnect will operate as a for-profit transmission company to which functional authority¹² over the PTOs' facilities will be transferred.

¹⁰See 18 C.F.R. § 385.214 (2002).

¹¹See *id.* at § 385.213 (a)(2).

¹²Applicants define functional authority as "Operational Authority, Pricing
(continued...)"

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PTOs will hold passive ownership interests in WestConnect and will not be able to participate in the day-to-day management of the RTO. All PTOs will have the right to transfer ownership of its assets to WestConnect for either cash or for equity in the RTO. In addition, WestConnect may invest in, construct, and own new transmission facilities. Participation as a PTO in WestConnect may be obtained through equity stakes, debt holder status, and non-contributory participation.

21. Equity ownership shares of WestConnect will be divided among Class A, B, and C interests based upon whether or not a member is a market participant.¹³ The WestConnect LLC Agreement provides that non-market participants will be assigned Class A ownership interests, upon providing capital contributions in the form of, among other things: (1) capital contributions to fund start-up costs; (2) transmission assets to WestConnect (divestiture); (3) capital contributions used by WestConnect for acquiring additional transmission assets; (4) capital contributions used to fund the operations of WestConnect transmission assets and/or provide new services; and (5) contributions made to fund the repayment of indebtedness. Class A interests will have the right to profit and loss distributions, active voting rights in the management of WestConnect, and the ability to elect their own members of the WestConnect Board of Directors (Board) upon sufficient ownership stake.¹⁴

22. Market participants, such as transmission-owning members, generators and power marketers that make capital contributions to WestConnect similar to those described for Class A interests, will be assigned Class C interests that have rights to profit and loss distributions but have no voting rights regarding the day-to-day management of WestConnect. Class C interests, however, will have limited voting rights on certain fundamental business decisions that are integral to the preservation of their financial

¹²(...continued)

Authority, Access Authority and Planning Authority." See WestConnect Tariff, Attachment 1, at 30.

¹³Applicants define market participant consistent with the definition in Order No. 2000. See WestConnect Tariff, Attachment 1, at 27.

¹⁴A Class A member may seat its own Board member upon acquisition of 12.5% (100% divided by 8 seats) of the total outstanding equity interests.

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interests.¹⁵ The voting rights attributable to Class C ownership interests will be assigned to an independent trustee as Class B Interests. The independent trustee, pursuant to an Independent Trustee Agreement, is obligated to vote the Class B interests consistent with the voting of the majority of the Board. Section 4.1(d)(iv) of the WestConnect LLC, proposes to allow Class C interests to modify the WestConnect LLC Agreement in order to increase their voting rights if these interests determine that the Commission's regulations have changed to allow for such greater voting rights.

23. Entities that may not hold equity positions in WestConnect, such as public power entities, and that transfer functional authority over transmission assets to WestConnect, along with contributions to fund start-up costs (or contributions after the date WestConnect commences operations), will be issued debt certificates and will be considered debt holders of WestConnect. Participants who receive debt holder status will not be considered an owner of WestConnect.¹⁶

24. The proposed WestConnect LLC Agreement and WestConnect TCA also allow transmission-owning entities to participate in WestConnect without being members or having debt holder status.¹⁷ A transmission owner may execute the WestConnect TCA,

¹⁵As discussed in more detail below, according to section 6.13 of the WestConnect LLC Agreement, absent a super-majority of the members, the Board may not: approve a merger with another entity other than an approved RTO; dissolve the company; convert the company into any other entity; make an initial public offering; institute bankruptcy proceedings; invest in any business not related to the transmission of electricity; or set, modify, or offer any equity compensation that exceeds compensation offered by a similarly situated entity.

¹⁶As with any publicly owned corporation, debt holders are considered creditors of the corporation, rather than owners.

¹⁷An entity that wishes to participate within the first two years of the independence date of WestConnect shall be required to become a member or debt holder, assuming that the entity satisfies certain financial and operational conditions. Applicants define independence date as "the date on which, after WestConnect Transmission Control Agreements and the WestConnect LLC Agreement have been executed, WestConnect commences performance of Functional Authority and other Regional Transmission Organization responsibilities." See WestConnect Tariff, Attachment 1, at 22. This

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comply with the application procedures, and pay the required fees under the WestConnect TCA to become a PTO. However, that PTO will not participate in ownership regarding voting and profit and loss distribution but will be subject to the rules of the WestConnect Tariff and operating requirements.¹⁸

25. Under section 3.5 of the WestConnect TCA, if a cooperative transmission owner is tax-exempt, WestConnect will become a member of the cooperative until either the WestConnect TCA is terminated or revenues from WestConnect become tax-exempt income pursuant to section 501(c)(12)(B) of the Internal Revenue Code.¹⁹

a. Intervenor Comments

26. Several intervenors argue that a for-profit RTO cannot truly meet the independence requirement of Order No. 2000. Basin asserts that an RTO should be accountable first and foremost to the public interest and that the for-profit structure is in conflict with that principle. NW Utilities, PNGC, and Public Power argue that a for-profit structure creates an incentive to favor transmission investment solutions over demand-side or generation-related solutions. Tri-State asserts that critical RTO functions (such as operating an RTO's markets, running an RTO's information systems, calculating , total transmission capability and available transmission capability, processing requests for transmission service and interconnection, and acting as the security coordinator) must be performed as objectively and transparently as possible and therefore the Commission should require that these functions be performed by a not-for-profit entity. Utah Municipals argues that a non-profit umbrella organization will have more support from

¹⁷(...continued)

requirement will not apply to federal RTO participants and cooperative transmission systems that have financing from the Rural Utilities Service.

¹⁸The WestConnect TCA will only become effective as to tax-exempt municipal transmission owners and cooperative transmission owners if approval for their participation is received by their respective authorities.

¹⁹Before executing the WestConnect TCA, transmission owners may request additional provisions in their particular WestConnect TCAs relating to tax matters. This will be determined by future tax analyses and possibly by advice requested from the Internal Revenue Service. Any tax language added to the WestConnect TCAs is not expected to alter the basic operating provisions of the WestConnect TCA.

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state commissions and will encourage the participation of public and federal power entities.

27. Certain intervenors argue that an aggregate of Class C interests could vote to modify the WestConnect LLC Agreement in order to increase their voting rights upon concluding that the Commission's regulations have changed to allow for such greater voting rights. Utah Municipals argues that the ability of Class A interests to combine interests in order to gain the voting power needed to replace a Board member gives the holders of Class A interests the ability to exercise direct control over the Board.

28. Arizona Consumer Systems contends that the equity ownership structure does not protect against various forms of indirect control by Applicants over voting interests of stock. It states that transfer of ownership will allow a PTO with Class C stock to transfer its interests to an independent person,²⁰ causing the Class C interests to become Class A interests. Arizona Consumer Systems maintains that the term "independent person" does not provide sufficient assurance against various forms of indirect control over stock by Applicants (for example, through trustees or informal proxies).

29. Duke argues that the requirement that the independent trustee vote the Class B interests in accordance with the majority of the Board dilutes the non-market participant Class A interests' influence on the Board and should not be allowed.

30. Southwest Transmission states that although it supports this proposal, many details have not yet been fully resolved. Specifically, the WestConnect market design may have a significant financial impact on Southwest Transmission's ability to retain its tax-exempt status. Southwest Transmission states that it cannot make a determination concerning its participation at this time, but it urges the Commission to accept the portions of the WestConnect TCA that allow WestConnect to become a member of a cooperative transmission owner so that Southwest Transmission may present this "acceptance" to the Rural Utilities Service to obtain needed tax assurances. Southwest

²⁰Applicants define independent person as "a natural person who is not a director, agent, officer or employee of any Market Participant and does not have direct financial interest in, nor stand to be financially benefitted in any transmission involving a Market Participant, except as provided in Article VII of the WestConnect LLC Agreement." See WestConnect Tariff, Attachment 1, at 27.

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Transmission also raises concerns regarding rate development and how the transmission revenue requirements will be recovered.

31. Salt River states that it has been involved in the WestConnect development process and requests that the Commission respect the balance resulting from the negotiations between jurisdictional and non-jurisdictional entities by allowing the participation of non-independent operating utilities.²¹

32. Western states that the transmission control agreement that it executes with WestConnect must allow Western to satisfy its statutory obligations, to comply with all relevant authorities, and to fulfill its mission to market reliable, cost-based hydropower to its customers.

b. Applicants' Response

33. Applicants state that the Commission explicitly addressed the issue of for-profit RTOs in Order No. 2000. According to Applicants, Order No. 2000 offers flexibility in choosing the form of corporate governance for an RTO, so long as it meets the Commission's independence requirement and other requirements. Applicants further state that in GridSouth,²² the Commission rejected claims that the transco form of an RTO should be rejected simply because it is opposed by some stakeholders in a region.²³

c. Discussion

²¹These include the use of a self-tracking system to match load to generation, right of first refusal to own new projects, acknowledgment that local regulatory boards determine revenue requirements, the honoring of transmission rights under existing agreements, and the recognition of the legal obligation of certain PTOs to first serve resident load customers (i.e., private use restrictions).

²²See GridSouth, 94 FERC ¶ 61,273 (2001).

²³See Applicants' Answer at 8.

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34. Order No. 2000 states that the Commission "will not limit the flexibility of proposed structures or forms of RTOs"²⁴ and concludes that the Commission is prepared to accept a transco, ISO, hybrid, or other form of an RTO as long as it meets our minimum characteristics, functions, and other requirements.²⁵ Accordingly, we accept the for-profit aspect of Applicants' proposal.

35. Applicants' proposal to allow Class C interests (i.e., market participants) to modify the WestConnect LLC Agreement in order to increase their voting rights is contrary to the independence requirement of Order No. 2000, because allowing Class C interests to unilaterally modify the WestConnect LLC Agreement would give them an undue preference over other shareholders; accordingly, Applicants must delete this provision. PTOs must first request that the Board modify that agreement and file with the Commission a modification to it. In addition, if the Commission's regulations change to allow for greater voting rights by Class C interests, those interests must request that the Board modify their voting rights and file such a change with the Commission.

36. We disagree with Utah Municipals' claim that the power of Class A interests (non-market participants) to replace a Board member could compromise the independence of the Board. In Order 2000, we stated that the decision making process of an RTO must be independent from market participants, because their economic and/or commercial interests are likely to be affected by an RTO's decisions and actions.²⁶ Because Class A interests are non-market participants, we find that allowing them to choose Board members is consistent with Order 2000 (i.e., this proposal satisfies the "threshold principle that [an RTOs] decisionmaking should be independent of market participants").²⁷ Furthermore, the requirement of an independent audit of the ownership structure mitigates the concerns of Utah Municipals and Arizona Consumer Systems concerning the possibility of various forms of indirect control over stock by Applicants.

²⁴Order No. 2000 at 31,036.

²⁵See id. In addition, the Standard Market Design NOPR adopts the Order No. 2000 independence requirements for an independent transmission provider.

²⁶See Order 2000 at 31,061.

²⁷Id. at 31,074.

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37. We also disagree with Duke's argument that the use of an independent trustee to vote Class B interests dilutes the voting rights of Class A interests. Because Class B interests will be voted by the independent trustee in accordance with the majority vote of the Board that voting will serve a purely ministerial function and therefore will not affect the outcome of issues that are sent to shareholders for a vote.

38. Finally, we find that Applicants' proposed business model encourages participation in WestConnect of various entities that are currently not participating and therefore will likely increase its scope. We recognize that there may be several statutory hurdles before participation of certain of these entities in WestConnect can be fully implemented, but we are encouraged by Applicants' flexibility towards the participation of these entities in WestConnect, through the construct of debt holder and non-contributory participant status.

2. Applicants' Proposal: Retained Rights

39. As noted, Applicants, as Class C interests, have proposed to reserve for themselves limited veto rights with respect to certain business decisions by the Board. As provided in section 6.13(b) of the WestConnect LLC Agreement (Limitations on Board Activities), these reserved rights include:

- The right to veto either mergers or acquisitions of another entity by WestConnect, except in the case of a proposed merger with another Commission-approved RTO;
- The right to veto a Board decision to dissolve WestConnect;
- The right to veto a Board decision to convert WestConnect into any other type of entity;
- The right to veto a Board decision to make an initial public offering;
- The right to block a Board decision to institute bankruptcy proceedings;
- The right to veto certain of the Board's decisions on equity compensation to the Board and other officers.

In addition, under the WestConnect TCA, unanimous consent of the PTOs is required for the Board to propose, before January 1, 2009, modifications to the transmission rate methodology.

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a. Intervenor Comments

46. Utah Municipals and Duke object to these retained rights, claiming that they compromise the independence of the Board. Utah Municipals also argues that the right to veto compensation decisions gives PTOs veto power over independent compensation decisions of the Board and notes that the Commission rejected a similar provision in GridSouth.

b. Applicants' Response

47. Applicants state that the Commission has recognized that passive owners may retain limited voting rights to protect their investment in transmission and in an RTO.²⁸ Applicants state that although the Commission has raised concerns over allowing passive owners to veto mergers and acquisitions, here the members do not have a veto power over mergers with other approved RTOs; therefore, their proposal allows for the expansion of geographic scope of WestConnect.

48. With respect to the retained right over equity compensation decisions, Applicants state that, unlike the proposal in GridSouth, their proposal is crafted to protect both the Board's independence and the financial interests of the investors. Passive members can only act when the Board's compensation exceeds what is customary for a company of its type and that they can only override the Board decision with a super-majority vote. Applicants further state that the Board may request that the Commission override the super-majority decision.

c. Discussion

49. We found in GridSouth that, with the exception of the reserved right to veto equity compensation determinations, it is appropriate for the PTOs, because of their commitment to turn over control of their assets to the RTO, to retain reserved rights concerning fundamental business decisions. Specifically, in GridSouth, the Commission permitted passive owners to retain certain veto rights, subject to two limitations. First, such rights must be exercised solely for the preservation of their capital investments in

²⁸See, e.g., Alliance Companies, 91 FERC ¶ 61,152 at 61,581-82 (2000).

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the RTO. Second, the use of such rights must be subject to the Commission's review.²⁹ Accordingly, we accept Applicants' proposed veto rights, subject to these same conditions. Furthermore, we expect the Board to make corporate decisions that are in the best interests of WestConnect, consistent with its fiduciary duties.

50. Section 6.13(b)(vi) of the WestConnect LLC Agreement provides for the following with respect to the compensation for Board members:

The Board shall not have the power to cause the Company to: set, offer, or modify compensation to, or of, or offer, enter into, amend, modify, or grant any equity under any equity option or other equity incentive plan with respect to the equity of the Company to or with any Director or Officer of the company that exceeds the compensation of directors or officers, respectively of companies of comparable size, business activity and credit standing.

51. In GridSouth, we rejected a condition similar to the one proposed by Applicants.³⁰ We stated that the control over equity-based compensation packages to the Board could compromise its independence and that the Board's fiduciary duty to protect the integrity of the members' capital contributions provides sufficient assurance to passive members concerning compensation. Applicants argue that the inclusion of the qualification that the Board's compensation cannot be "in an amount that exceeds compensation for directors of companies of the same size and character" distinguishes their proposal from that in GridSouth. However, Applicants' proposed qualification does not take control over the Board's compensation out of the hands of the PTOs. Furthermore, the Commission does not want to be an arbitrator on compensation issues, as contemplated by the WestConnect LLC Agreement; these are business decisions best handled by the Board. Accordingly, we reject the right of the PTOs to veto equity compensation decisions.

²⁹See GridSouth, 94 FERC at 61,986 (stating that if a passive owner is dissatisfied with a merger or consolidation decision by the independent Board, it must come to the Commission and affirmatively demonstrate that the proposed merger or consolidation will undermine the integrity of its investment).

³⁰See id. at 61,986-87.

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3. Applicants' Proposal: Compliance Audits of Passive Ownership Interests

52. Applicants propose, as required by Order 2000, that an independent audit be performed of the passive ownership interests two years after the approval of WestConnect as an RTO. Appendix H of the WestConnect Tariff (Market Monitoring) provides that an audit of the passive ownership interests must be prepared by the independent market monitor, as provided for in the WestConnect LLC Agreement.³¹ This audit must include examining whether any class or group of classes of market participants is able to gain an undue competitive advantage through its voting rights or other rights to participate in WestConnect's decisions or actions.³² Appendix H of the WestConnect Tariff further states that WestConnect shall provide appropriate staffing and resources for the Market Monitoring and WestConnect Tariff Compliance Unit (Market Monitoring Unit).³³ Section 7(b) of Appendix H (Market Monitoring and Tariff Compliance Unit and Market Advisor) states that the Market Monitoring Unit shall be subject to the management oversight of the CEO. Accordingly, the Market Monitoring Unit will be an operating division of WestConnect.

a. Discussion

53. In Order No. 2000, the Commission required RTOs with passive ownership interests to propose a process for an independent compliance audit to ensure the independence of the decision-making process of the RTO from passive owners.³⁴ Order No. 2000 concluded that the auditor may not be affiliated with the RTO or its owners.³⁵ Accordingly, Applicants must modify their proposal to clarify that the audit of the ownership structure will be performed by an independent entity (i.e., not affiliated with or, in any way, under the control of WestConnect or its market participants).

³¹See Applicants' Transmittal Letter at 16.

³²See WestConnect Tariff, Appendix H, Section 2(b)(viii) (Definition of Market Monitoring).

³³See id. at H.7(a).

³⁴See Order No. 2000 at 31,066.

³⁵See id. at 31,067.

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4. Applicants' Proposal: Governance

54. The WestConnect LLC Agreement provides that WestConnect will be governed by an independent Board consisting of nine directors. Directors are prohibited from having either a financial interest in or business relationship with Applicants or any other market participant. Directors, among other things, must have senior executive level experience and must perform pursuant to a code of conduct.³⁶ In addition, directors owe fiduciary duties to WestConnect members.³⁷ WestConnect may hire former employees of market participants, but these employees must divest any equity interest and any other financial interests in their former employers within six months of their employment with WestConnect.

55. A Board Selection Committee will select a nationally recognized executive search firm to establish a slate of 24 candidates for the Board. Each PTO is entitled to one seat on the Board Selection Committee, while stakeholders from seven other stakeholder sectors³⁸ will choose a single representative each to represent their respective sectors. The Board Selection Committee is then divided into two voting groups: PTOs and the group comprised of the representatives from the remaining seven stakeholder sectors. If the two groups are unable to select eight Board candidates by consensus, the Board Selection Committee will identify those candidates that the PTOs' and stakeholders' representatives have agreed on and a series of rotating preemptory strikes will be used to narrow the slate of the remaining potential candidates. This process will continue for up to eight strikes, depending on how many candidates have already been agreed upon, until the Board Selection Committee has reduced the slate of candidates to eight (*i.e.*, when the number of candidates that were agreed upon are added with those reached through the preemptory strike process). The resulting eight candidates will then be offered seats on the initial Board. These eight Board members will then select the ninth Board member, who will serve as president and chief executive officer (CEO) of WestConnect.

³⁶The WestConnect code of conduct is included as Appendix R of the WestConnect Tariff (Code of Conduct).

³⁷Section 6.19 of the WestConnect LLC Agreement expressly excludes from the scope of fiduciary duties any duty to consider the interests of the passive owners beyond WestConnect's transmission business.

³⁸The Applicants propose eight stakeholder classes. See infra P 43.

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56. Applicants propose to establish a Stakeholder Advisory Committee that will consist of two representatives from each of the following eight groups: (1) transmission owners; (2) load serving entities; (3) generators; (4) transmission-dependent utilities; (5) power marketers; (6) large retail customers; (7) small retail customers; and (8) utilities commissions. A market participant and any of its affiliates may only participate in one of the stakeholder groups. To avoid conflict with their duties as regulators, the representatives from the utilities commissions will not have any voting rights. The Stakeholder Advisory Committee will have the right to present to the Board proposed changes to the WestConnect Tariff if the changes are approved by a two-thirds vote of the Stakeholder Advisory Committee. Stakeholders that seek to designate a representative to the Stakeholder Advisory Committee must pay an initial fee of \$10,000 and make an annual payment of \$5,000.

a. Intervenor Comments

57. Intervenors argue that the Board selection process enables PTOs to seat a Board that would favor their interests. They assert that the strike process favors PTOs, who collectively will exercise eight strikes, while the remaining seven stakeholder sectors must agree on eight strikes, giving 50 percent of the votes in the selection process to PTOs. Therefore, intervenors assert that the process unfairly gives preference to PTOs.

58. Nevada Coalition claims that a more equitable process will be to create a Board Selection Committee consisting of two representatives from each stakeholder group, which selects Board candidates based on a majority vote. It also states that there is a lack of detail in Applicants' proposal regarding who is eligible to be a stakeholder. NRG argues that contrary to Applicants' claim, the selection process is not consistent with GridFlorida.³⁹

59. Some of the intervenors claim that the role of the Stakeholder Advisory Committee should be expanded. They argue that the Stakeholder Advisory Committee should be able to bring any issue to the Board, not just proposed modifications to the WestConnect Tariff. These intervenors also argue that individual stakeholders and stakeholder groups should be allowed to bring "minority statements" to the Board without a super-majority vote. In addition, Western Trading and Dynegy assert that the

³⁹GridFlorida, LLC, 94 FERC ¶ 61,020 (2001) (GridFlorida).

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Board and the Stakeholder Advisory Committee should be developed as soon as possible so that stakeholders have input in developing the organization.

60. Enron and Tractebel argue that PTOs can exert control over who may participate in a stakeholder group. They also state that there is a lack of detail regarding who is eligible to be a stakeholder.

b. Applicants' Response

61. Applicants contend that the Board selection process proposed is virtually identical to the one the Commission accepted in GridSouth and that a similar process was approved by the Commission in GridFlorida. They state that, as in GridSouth and GridFlorida, the Board selection process: uses an independent search firm to identify candidates for the Board, who must be independent from all market participants; provides for a Board Selection Committee; and uses peremptory challenges rotating between Applicants and other stakeholders to eliminate candidates if the Board Selection Committee does not reach a consensus on candidates.⁴⁰

62. In response to the issues raised regarding the Stakeholder Advisory Committee, Applicants assert that the Commission has determined that the process by which the Board and stakeholders communicate should be developed by the Board, once it is in place, with stakeholder input.⁴¹

c. Discussion

63. In Order No. 2000, the Commission stated that "the principle of independence is the bedrock upon which the ISO must be built" and that this standard should apply to all RTOs, whether they are ISOs, transcos, or variants of the two.⁴² Furthermore, we stated in Order No. 2000 that we require a collaborative process in the development of RTOs and that any proposed RTO governing board be independent in both perception and reality. The Commission finds, subject to the modifications discussed below, that the

⁴⁰See Applicants' Answer at 13.

⁴¹See Applicants' Answer at 13 (citing Carolina Power & Light Company, et al., 94 FERC ¶ 61,273 at 61,984 (2001) (GridSouth)).

⁴²See Order No. 2000 at 31,047.

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Applicants' proposal for selecting the Board will result in an independent Board of Directors.

64. We require the following two modifications to Applicants' proposal to preclude a voting advantage in the board selection process. First, we require that two representatives from each of the stakeholder groups, including PTOs, serve on the Board Selection Committee. Under the proposal, PTOs will have a voting advantage because the proposal allows all PTOs to participate on the Board Selection Committee while only one representative from each of the seven remaining stakeholder groups may participate in the Board Selection Committee voting. However, we further require, because the Applicants' proposal is not clear on the matter, that to avoid conflict with their duties as regulators, the representatives from the utilities commissions will not have any voting rights on the Board Selection Committee, as is the case on the Stakeholder Advisory Committee.

65. Second, we direct Applicants to develop a revised process for the selection of candidates that elects them based on a majority of the vote. Contrary to Applicants' assertion, their proposal is not identical to those accepted in GridFlorida and GridSouth. The proposals in GridFlorida and GridSouth used a majority-of-the-stakeholders vote process, which was employed after the slate of candidates was selected by the search firm.⁴³ Applicants here request that the preemptory strikes be divided up between the PTOs and the remaining stakeholders which gives 50 percent of the votes in the selection process to Applicants, who collectively represent only one of the eight stakeholder groups.

66. The use of a simple majority vote will ensure a collaborative decision-making process and eliminate the perception and/or the possibility that PTOs will have undue influence over the Board because of their disproportionate ability to choose its members.⁴⁴

⁴³See GridFlorida, 94 FERC at 61,046; GridSouth, 94 FERC at 61,988.

⁴⁴See, e.g., Entergy Services Inc., 88 FERC ¶ 61,149 at 61,501 (1999) (stating that the Commission finds it acceptable to use a stakeholder committee for board selection, assuming the committee is fair and balanced and does not allow any one type of customer to veto particular candidates).

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67. Enron notes that section I.1 of Schedule D of the WestConnect LLC Agreement dictates that the Board Selection Committee will be established consistent with the principles set forth in section 6.1 of the WestConnect LLC Agreement (Board of Directors). However, that section does not contemplate the development of the Stakeholder Advisory Committee; instead, the Stakeholder Advisory Committee is developed pursuant to section 6.7 of the WestConnect LLC Agreement (Stakeholder Advisory Committee and Other Stakeholder Committees). Accordingly, we require Applicants to revise section I.1 of Schedule D of the WestConnect LLC Agreement (Board Selection Process) to reference the correct section of the WestConnect LLC Agreement.

68. Enron and Tractebel argue that PTOs may exert control over the Board Selection Committee by dictating who may be an eligible stakeholder and in which stakeholder sector an eligible stakeholder may participate. According to section I.3 of Schedule D of the WestConnect LLC Agreement, the initial members and debt holders of WestConnect "shall have the right to reject any entity choosing to participate in a sector, after giving notice and an opportunity to be heard by such entity, on the grounds that such entity does not satisfy the criteria for membership on the Board Selection Committee or in the sector chosen by such entity." Section 6.7(a) of the WestConnect LLC Agreement provides the criteria for who may be a stakeholder.⁴⁵ Those criteria should not be subject to the interpretation by PTOs; therefore, we direct Applicants to remove the above quoted language from section I.3 of Schedule D.

69. We expect the Board, when seated, to consider all issues raised by the stakeholders. Such an open dialogue is key to the formation and the development of WestConnect. Therefore, the WestConnect LLC Agreement must not limit the ability of stakeholders, absent a quorum of the Stakeholder Advisory Committee, to raise issues before the Board. We direct Applicants to modify section 6.7 of the WestConnect LLC Agreement accordingly.

70. Applicants' proposal to develop eight stakeholder classes does not allow for the participation of all potential stakeholders. Therefore, we require that Applicants add two additional stakeholder classes to ensure that all stakeholders are represented on the Stakeholder Advisory Committee. These two classes are public interest organizations

⁴⁵The definition of each stakeholder group is included in Applicants' Master Definition List. See WestConnect Tariff, Attachment 1.

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(e.g., consumer advocates, environmental groups and citizen participation) and alternative energy providers. The inclusion of these classes of stakeholders will provide all interested parties with the ability to participate in the development of WestConnect.

71. With respect to the issues regarding the lack of clarity in who may participate in each stakeholder class, we find that the definitions included in the Master Definitions List of the proposed WestConnect Tariff provides sufficient detail regarding who is eligible to be a stakeholder. However, we recognize that, pursuant to our requirement to add two additional stakeholder groups, Applicants may need to modify definitions to obtain the appropriate delineation of one group over another (e.g., generators and alternative energy providers). Furthermore, as discussed earlier, we find that the definition of the stakeholder groups should not be subject to interpretation by the Applicants. Accordingly, in order to develop clear stakeholder group definitions and eligibility requirements, Applicants, along with interested stakeholders, should develop the necessary clarity and standards.

D. RTO Characteristic No. 2: Scope and Regional Configuration

The RTO must serve an appropriate region.

1. Applicants' Proposal

72. Applicants claim that WestConnect will have sufficient scope and regional configuration. They state that WestConnect is designed to have functional authority over transmission assets in Arizona, New Mexico, West Texas, Nevada, Wyoming, and Colorado.⁴⁶ Applicants contend that this has historically been a market area for wholesale trading.

73. Applicants state that they have designed an RTO structure that offers flexible participation options and that can be expanded to include other transmission systems in the West, including participation by federal, public power, and cooperatively owned entities. Therefore, they assert that the WestConnect proposal may serve as a platform for other RTO development in the West and, thus, help facilitate a West-wide RTO.

⁴⁶Applicants' assertion is based upon the expected participation of Western, Southwest Transmission, and Salt River. A map of the control areas of Applicants is included in Appendix C of this order.

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a. Intervenor Comments

74. Several intervenors favor a single RTO in the Western interconnection but agree that multiple RTOs in that region may be needed initially.

75. US Executive Agency, Tri-State, Navajo, and Utah Municipals state that an RTO that includes only Arizona and New Mexico is too small to be considered a stand-alone RTO region. Furthermore, Tri-State argues that although Applicants serve a majority of the load in the states of Arizona and New Mexico, they do not encompass most of the geographic area in those states. Utah Municipals argues that the proposal does not adequately provide for public power participation and therefore a significant amount of transmission facilities in the region are excluded. Utah Municipals also asserts that the proposal contains barriers to new membership by requiring that any utilities that join after the independence date⁴⁷ bear the full cost of their integration into the WestConnect system.

76. Tri-State and Navajo assert that many of the physical and engineering problems in the West with respect to energy flow require a much larger RTO and that these problems cannot simply be treated as seams issues. Furthermore, Tri-State notes that WestConnect will have no participants in Colorado.

77. NRG claims that the WestConnect proposal fails to satisfy the requirements of Order No. 2000 because it does not further the development of greater regional integration or regional energy markets. NRG asserts that an RTO must advance a seamless market through the entire Western interconnection.

78. Arizona Consumer Systems argues that WestConnect does not possess sufficient scope because bulk power and transmission trading data demonstrate that the actual scope of the relevant regional markets extends beyond the borders of the proposed WestConnect grid.

79. PNGC and NW Utilities assert that the Commission should only consider the WestConnect proposal for the Southwest, arguing that the expansion of the WestConnect proposal geographically will hinder the development of RTO West.

⁴⁷See supra note 17 and accompanying text.

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b. Applicants' Response

80. Applicants disagree that the proposed geographic region covered by WestConnect is not large enough to satisfy Order No. 2000. They state that Western, Salt River, and Southwest Transmission have been active participants in creating the WestConnect proposal. They also recognize that an RTO in the Southwest may be an island among public power entities unless cooperative solutions are developed with public power entities.

81. Applicants contend that the differing proposals in the Northwest and the Southwest reflect a longstanding separation of planning and operations and differing system configurations between the two regions. The electric systems in the Northwest and in the Southwest have been distinct market areas with their own reserve sharing arrangements, generating facilities, and extra-high voltage transmission lines. Thus, the electric systems in the Northwest and the Southwest have typically operated as two distinct regions, because the weak transmission ties between them limit their trading capability.

82. In addition, Applicants state that they are not opposed to the consolidation of RTOs in the West and urge the Commission to allow them to move forward with their RTO proposal, while encouraging discussions among WestConnect, RTO West,⁴⁸ Transconnect,⁴⁹ and TRANSLink.⁵⁰

c. Discussion

83. We find acceptable Applicants' proposal for developing an RTO that includes all public utilities located in the Southwest and allows for participation by non-public utility entities in that area. We are encouraged by the participation of non-public utility entities, such as Western, Salt River, and Southwest Transmission, in drafting the proposal, because we believe that the participation of these entities and all other non-public utility entities located in that region would be beneficial to increasing efficient transmission in

⁴⁸See Avista Corp., et al., 100 FERC ¶ 61,274 (2002) (RTO West).

⁴⁹See Avista Corp., et al., 100 FERC ¶ 61,297 (2002) (Transconnect).

⁵⁰See TRANSLink Transmission Company, L.L.C., et al., 99 FERC ¶ 61,106 (2002) (TRANSLink).

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the Southwest.⁵¹ We note that the governance structure for WestConnect has been developed to accommodate participation by non-public utility entities without affecting their status. We encourage Applicants to continue their dialogue with all transmission owners in the region to further expand the scope of WestConnect.

E. RTO Characteristic No. 3: Operational Authority

The RTO must have operational authority for all transmission facilities under its control.

1. Applicants' Proposal

84. Applicants propose to consolidate the management of the control area functions and assume authority over the physical control area operator responsibilities for the region in which WestConnect will operate, but they will maintain the local control areas and their respective operations centers.⁵² Under the operational authority⁵³ of WestConnect, PTOs will physically execute control area operations through their area operations centers; thus, area operations centers will be the primary means through which WestConnect will implement its operational authority over the transmission facilities of

⁵¹For example, Western has approximately thirty-six interconnections with numerous entities located in Utah, Colorado, New Mexico Arizona, and Nevada and nine direct interconnections into Southern California. See Western 2000 Service Operations Survey at <http://www.wapa.gov/media/pdf/2000OpsSum.pdf>.

⁵²Applicants' proposal is not clear as to whether WestConnect will become one single NERC-approved control area.

⁵³Applicants define operational authority as "(a) the rights of WestConnect Tariff to direct the Participating TOs how to operate their "Operational Authority Facilities for the purpose of affording comparable, non-discriminatory transmission access and meeting Applicable Reliability Criteria; and (b) the rights of WestConnect under the Generator Agreements, the Scheduling Coordinator Agreements and the WestConnect Tariff to issue Dispatch Instructions to Generating Units and Dispatchable Demands in accordance with Appendix C (Dispatch and Emergency Operations) to the WestConnect Tariff." See WestConnect Tariff, Attachment 1, at 31.

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PTOs. Applicants also propose to develop a self-tracking system⁵⁴ under which certain metered systems may schedule and provide service within that system. In addition, Applicants state that they are investigating whether to use the security coordinator already established for the region or to have WestConnect perform the security coordinator function.

a. Intervenor Comments

85. Intervenors state that because some operational duties are assigned to market participants, WestConnect will not have sufficient operational authority. Other intervenors assert that the proposal lacks specificity regarding what facilities will be under the operational authority of WestConnect.

86. Specifically, EPSA asserts that the proposal improperly allows PTOs to retain control area functions. EPSA states that the use of a self-tracking system enables PTOs to: calculate their own demand forecast when submitting net interchange schedules; self-supply energy imbalances; dispatch their own regulation; self-supply load following; supplement energy; and shift generation within different resources. EPSA concludes that this frees PTOs from balancing energy and ancillary service obligations (which are imposed on all other market participants) and, therefore, is contrary to Order No. 2000.

87. Arizona Consumer Systems asserts that there is no assurance⁵⁴ that the sharing of operational authority among WestConnect and PTOs will neither adversely affect reliability nor provide any market participant with an unfair competitive advantage. Arizona Consumer Systems states that too much physical operational control remains with PTOs.

88. NW Utilities, Arizona Consumer Systems, Utah Municipals, and Nevada Coalition note that the proposal fails to identify the transmission facilities that WestConnect will have under its functional control. Arizona Consumer Systems argues that the proposal allows Applicants to pick which of their facilities they will allow WestConnect to control. It points out that there is no requirement that PTOs place all of

⁵⁴A self-tracking system is defined by Applicants as "a portion of the WestConnect Grid completely bounded by Real-Time metering that enables the Scheduling Coordinator to match the aggregate Generation within such portion of the WestConnect Grid to the aggregate Demand within such portion of the WestConnect Grid on a second-by-second basis." See WestConnect Tariff, Attachment 1, at 39.

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their transmission facilities, all of their facilities at or above a certain voltage level, or any of their facilities under WestConnect's functional authority. Nevada Coalition argues that the Commission should require that WestConnect have operational authority over all Commission-jurisdictional services and all facilities used in providing such services.

89. According to Utah Municipals, the WestConnect TCA does not list the facilities or specify criteria to identify which facilities will be put under WestConnect's control. It further argues that there is a lack of specificity in certain definitions in the WestConnect Tariff, which could lead to different understandings as to which facilities are under the control of WestConnect and for what purposes. Utah Municipals also asserts that Applicants have not shown that their hierarchical control structure (*i.e.*, area operations centers operating under the direction of WestConnect) will not undermine WestConnect's operational control or allow discriminatory operation.

90. Nevada Coalition maintains that WestConnect is not sufficiently independent from PTOs because they retain much of the responsibility for system dispatch and control area operations. For example, the WestConnect Tariff provides that area operations centers may perform some of the dispatch functions of the RTO.⁵⁵ Nevada Coalition asserts that this delegation of responsibility needs to be restricted so that WestConnect retains operational authority. Nevada Coalition claims that the proposed standards of conduct do not apply to area operations centers and regional operations centers and, as a result, problems will arise regarding information security and separation of transmission and generation functions between the area operations centers and regional operations centers.

91. Duke argues that the WestConnect TCA restricts the ability of WestConnect to independently operate the grid. According to Duke, the WestConnect TCA contains numerous requirements that WestConnect consult with PTOs before taking action, and therefore, WestConnect cannot unilaterally revise its operating procedures.⁵⁶

⁵⁵See WestConnect Tariff, Appendix C, Section 1.4 (Dispatch and Emergency Operations, Responsibilities and Authorities). For example, section C.1.4(c) states: "as agreed upon by WestConnect and a Participating TO, through predetermined procedures or delegation of authority, some of the above activities may be performed by that Participating TO's [area operations centers] without specific dispatch instructions issued by WestConnect." *Id.*

⁵⁶See Duke at 8, referencing section 5.1 of the WestConnect TCA (Rights and
(continued...)

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b. Applicants' Response

92. Applicants assert that PTOs will not retain all existing control area functions. WestConnect will become the control area operator for the WestConnect region and will perform those control area functions that are not performed by a self-tracking system. Applicants further state that the WestConnect TCA provides that PTOs will turn over their control area functions to WestConnect.

93. Applicants clarify that any scheduling coordinator can qualify as a self-tracking system if it meets certain criteria, but the scheduling coordinator will still have to: settle with WestConnect; respond to dispatch instructions; provide balanced schedules; remain exposed to balancing energy obligations and penalties; and self-supply to or receive from WestConnect the remaining ancillary services. Accordingly, a scheduling coordinator's operation of a self-tracking system allows it to "dynamically" schedule its current control area.

94. Applicants state that the ability to self-supply their customers is critical to the involvement of public power participants. They contend that the self-tracking system will allow a scheduling coordinator to minimize balancing energy charges from WestConnect, is equitable to everyone, and allows those utilities that have obligations to supply native load customers to serve such customers at cost using their own generation resources. Applicants also state that this benefits WestConnect and, therefore, its customers by reducing the amount of load following and regulation needed by WestConnect in order to meet load and maintain reliability.

c. Discussion

95. In Order No. 2000, we stated that an RTO must have clear authority to direct all actions that affect the facilities under its control, including the decisions and actions taken at any satellite control centers.⁵⁷ Applicants' proposal contains certain instances where operational actions may not be directly ordered by WestConnect. For example, area

⁵⁶(...continued)
Responsibilities of WestConnect, Promulgation of Certain WestConnect Grid Arrangements).

⁵⁷See Order No. 2000 at 31,090-91.

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operations centers may issue dispatch instructions and perform switching of physical facilities without instructions from WestConnect.⁵⁸ In addition, Appendix C of the WestConnect Tariff states that area operations centers may control generation that is not under the control of WestConnect for ancillary service requirements in order to control voltage support.

96. While we agree that the elimination of directions from multiple control area operators will assist in avoiding seams within WestConnect due to the divergent control area operations protocols, we note that the procedures by which the area operations centers will act have not yet been determined. Accordingly, Applicants must explain exactly what authority the area operations centers will be delegated. Absent such details, we are unable to determine whether Applicants' proposal meets the requirement of operational authority under Order No. 2000. Therefore, we conditionally accept Applicants' proposal, subject to our acceptance of such protocols.

97. We agree with the concerns raised by EPSA regarding Applicants' proposed self-tracking system. A participant that is granted self-tracking system status may act operationally without direction from WestConnect. Although Applicants state that a self-tracking system must still respond to WestConnect, there is insufficient detail regarding what authority a self-tracking system may have outside of WestConnect's operational authority.⁵⁹ Accordingly, we require Applicants to explain in detail the effect of a self-tracking system on the ability of WestConnect to provide transmission service and operate the energy markets it oversees.

98. We disagree with Nevada Coalition that the area operations centers will not be subject to the proposed standards of conduct. Pursuant to the tariff, if an area operations center issues dispatch instructions from WestConnect to a scheduling coordinator, the area operations center, among other things, must meet the standards of the conduct

⁵⁸See Sections C.1.3 and C.1.4 of Appendix C of the WestConnect Tariff

⁵⁹See, e.g., WestConnect Tariff, Appendix C, Section 7.6.2 (Dispatch of Balancing Energy stack) (stating that a self-tracking system is responsible for the dispatch of its own regulation, load following up, load following down, and supplemental energy requirements).

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requirements of the Commission and those set forth in Appendix R to the tariff.⁶⁰ However, as discussed above, since we require more information regarding the delegation of operational authority to area operations centers, we require Applicants to state clearly that the area operations centers must adhere to the WestConnect standards of conduct.

99. Applicants state that WestConnect will be in an area in which security coordination is currently being provided by the Rocky Mountain Desert Southwest Security Center, which is within the Western Electricity Coordinating Council. They further state that they are in the process of determining whether to use this existing security coordinator for the region or to have WestConnect become the security coordinator for the region. Order No. 2000 requires that an RTO be the security coordinator for its region. If Applicants decide to contract out the security coordinator responsibilities to a third party (e.g., the Rocky Mountain Desert Southwest Security Center), they must notify the Commission that they are using such an entity.⁶¹

100. We note that Applicants have not specified what transmission facilities will fall under the operational authority of WestConnect. Any decision on what transmission facilities will be under the authority of WestConnect shall be subject to the review of the Commission. In a future filing, Applicants must provide a complete listing of the transmission facilities that will be under WestConnect's operational control and the facilities that will remain under the operational control of each PTO. In addition, Applicants must provide a rationale for excluding any transmission assets that provide transmission service from WestConnect's operational control. We encourage Applicants to continue working with all stakeholders in the region in order to determine the appropriate facilities to be placed under WestConnect's operational authority. We also emphasize the Commission's requirement that RTOs provide for one-stop shopping for transmission service. Transmission customers must be able to request transmission service only from WestConnect, rather than from WestConnect and PTOs.

F. RTO Characteristic No. 4: Short-Term Reliability

The RTO must have the exclusive authority for maintaining the short-term reliability of the grid it operates.

⁶⁰See Section C.1.4(g) of Appendix C.

⁶¹See Order No. 2000 at 31,090-91.

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1. Applicants' Proposal

101. Applicants state that all uses of the WestConnect grid will be scheduled through WestConnect. Schedules must be submitted whether they are for transmission service or for using rights under non-converted existing contracts. WestConnect will have the authority to curtail schedules and issue dispatch instructions. In addition, all maintenance schedules must be coordinated through WestConnect.

102. Under the WestConnect Tariff, Applicants state that WestConnect will have the exclusive authority: (1) for receiving, confirming, and implementing all schedules; (2) to order redispatch of any generator connected to the WestConnect Grid; and (3) over requests for outages of transmission facilities and the generating units providing local generation resource services.

a. Intervenor Comments

103. Intervenors question the ability of WestConnect to implement short-term reliability measures as a result of its sharing of operational authority with PTOs.

b. Discussion

104. Order No. 2000 requires that RTOs have exclusive authority for: (1) receiving, confirming, and implementing all interchange schedules; (2) redispatch for any generator connected to its transmission facilities; and (3) approval and disapproval of all requests for scheduled outages of transmission facilities to ensure that the outages can be accommodated within established reliability standards.⁶² Based on our findings and required modifications regarding WestConnect's proposal for operational authority through a hierarchical control structure, we find that WestConnect's ability to maintain short-term reliability will not be impaired.

105. WestConnect will have scheduling authority for all transactions, including existing contract service. With respect to its ability to redispatch generation, WestConnect, through the application of its proposed Generator Agreement, requires generators which are interconnected with the WestConnect grid and who wish to participate in any of the

⁶²See Order No. 2000 at 31,104.

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WestConnect markets to submit to mandatory scheduling and redispatch.⁶³ Finally, pursuant to the tariff and the Generator Agreement, WestConnect will require the coordination of all transmission and generator outages and have rejection authority over scheduled outages if such outages may impair WestConnect operations.⁶⁴ Accordingly, we find that Applicants' proposal meets the requirements of Order No. 2000 for short-term reliability.

G. RTO Function No. 1: Tariff Administration and Design

The RTO must administer its own Tariff and employ a transmission pricing system that will promote efficient use and expansion of transmission and generation facilities.

106. Applicants propose that WestConnect will have the authority to design and administer its tariff. The WestConnect TCA provides WestConnect with the exclusive right and obligation to provide transmission service across the WestConnect transmission system, to develop the pricing of transmission and ancillary services under the tariff, and provide access to transmission through interconnection of generation and load to the system.

107. We find that, subject to the modifications required below, WestConnect will meet the requirements of Order No. 2000 for Tariff Administration and Design. We also direct certain modifications to Applicants' proposal for processing interconnection requests. Specific elements of Applicants' tariff design proposal are discussed in more detail below, including further guidance that will ensure that WestConnect independently administers its tariff.

1. Applicants' Proposal: Contract Conversion

108. WestConnect will be the sole provider of transmission service over all facilities under its operational authority. For this reason, WestConnect will manage transmission service obligations under existing transmission contracts and load service obligations that

⁶³See Section 9.3 of the WestConnect Tariff and Section 4.2.3 of the proposed Generator Agreement.

⁶⁴See Appendix F of the WestConnect Tariff.

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are not converted to WestConnect service as well as converted transmission service obligations.

109. The WestConnect Tariff recognizes four types of existing agreements: (1) Type 1 contracts: existing contracts between PTOs that provide for transmission service only; (2) Type 2 contracts: existing contracts between PTOs that provide multiple services, including transmission service and exchanges; (3) Type 3 contracts: existing contracts between a PTO and a load serving entity that is not a PTO (e.g., a transmission dependent utility); and (4) Type 4 contracts: existing contracts between a PTO and a generator and/or power marketer, including those that are affiliated with a PTO.

110. Applicants propose that conversion of Type 1 contracts to service under the WestConnect Tariff will be mandatory. Conversion of Type 2 contracts will not be mandatory, but the parties to these contracts must make their best efforts to convert them to service under the WestConnect Tariff. Type 3 and Type 4 contracts will not be required to convert to WestConnect Tariff service unless required by the terms of the existing contract, law, or by order of the Commission.

111. Type 1 contracts, when converted, and Types 2 and 4 contracts, if converted, will be subject to mandatory negotiated transfer payments that will be made by the existing contracts transmission rights holder to the PTO providing the transmission service. Appendix E provides that this payment will reflect the payment terms that will have existed in the absence of the conversion and will be adjusted to reflect changes in the value of the existing contract to the parties as a result of the conversion. The transfer payment will be made for the remaining term of the converted contract. If the parties are unable to agree on the transfer payment, the dispute will be handled by WestConnect's alternative dispute resolution process (WestConnect ADR). Transfer payments made by or received by PTOs will be required to be reflected in PTOs' revenue requirements. In addition, converted existing contracts will be entitled to firm transmission right auction revenues. Applicants state that transfer payments reduce cost shifting as a result of removing transmission service from WestConnect.

112. Upon conversion, service under Type 3 contracts will take WestConnect transmission service and pay all of the applicable charges under the WestConnect Tariff. If a converted Type 3 contract has a fixed term or the rights holder has the right of first refusal under the converted existing contract or under Order No. 888, the rights holder will be entitled to the firm transmission rights auction revenues for the MW amount of the converted existing contract through the term of that agreement. The existing contract

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rights holder will have rights to the firm transmission rights auction revenues for a minimum of 5 years after WestConnect commences RTO operations, if the rights holder under the existing contract gives notice of termination in accordance with the existing contract no later than 60 days after the independence date. If notice of termination is not given within 60 days, then the rights holder will have rights to firm transmission rights auction revenues only until the end of the term of the existing contract.

113. Contracts that are not converted will be managed by WestConnect, pursuant to the terms of the non-converted contract, but will not take service under the WestConnect Tariff. In order to fulfill the obligations under non-converted existing contracts, the WestConnect Tariff provides that WestConnect will compile, as provided by PTOs with existing contracts to WestConnect, non-converted rights instructions in order to honor the non-converted existing contract.⁶⁵ The non-converted rights instructions will be used to ensure that the allocation, scheduling, redispatch, and curtailment priorities of the non-converted existing contract transmission services are maintained in compliance with the non-converted contract and will be handled in proper relationship to WestConnect transmission service as provided for under the WestConnect tariff.

114. All non-converted rights instructions will be posted on WestConnect's website, will reflect sufficient detail that will enable WestConnect to implement the instructions, and will enable any other party to fully ascertain the asserted rights and priorities of the non-converted existing contract.

115. The WestConnect tariff provides that any parties to a non-converting existing contract will be able to agree at any time to convert them to WestConnect transmission service.

a. Intervenor Comments

116. Tri-States contends that very little emphasis has been placed on preserving the rights of existing customers under their contracts. Arizona Consumer Systems argues that WestConnect's proposal unduly discriminates against transmission dependent utilities with existing transmission contracts. According to Arizona Consumer Systems, will pay

⁶⁵The data requirements to be submitted in a non-converted rights instruction are included in Section E.5.3 of Appendix E to the WestConnect tariff (NCR Instruction Date Requirements).

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multiple rates under the initial pricing structure by continuing to pay the existing contract rates in addition to a PTO's access area rate. NW Utilities comments that pre-existing firm transmission rights must be guaranteed, regardless of whether transmission customers convert to RTO service or remain customers of the incumbent transmission owners.

b. Applicants' Response

117. Applicants respond that there are no penalties for customers taking service under non-converting, existing service agreements. These customers will continue to pay in accordance with the terms of the existing contracts until these contracts terminate.

c. Discussion

118. Applicants propose that the mandatory conversion of existing contracts be limited to transmission-only arrangements between participating utilities (i.e., Type 1 contracts).⁶⁶ There is not a mandatory contract conversion requirement for all other contracts. However, if the terms of a non-converted existing contract permits the PTO to refuse to renew or refuse to extend the term of the existing contract, the PTO will be required to refuse any renewal or extension of the term of the transmission service under the existing contract at the earliest possible date, in order to facilitate conversion to WestConnect tariff service. Accordingly, except for conversion of Type 1 contracts, the Applicants propose a voluntary existing contract conversion process.

119. In Order No. 2000, the Commission adopted a measured approach to the treatment of existing contracts. We stated that the treatment of existing transmission contracts was to be reviewed on a case-by-case basis and that each RTO could propose whatever contract reform it thought was necessary. The Commission emphasized that the goal in reviewing existing transmission contracts and contract transition plans is to balance respect for existing contractual arrangements against the need for uniform transmission

⁶⁶The Standard Market Design NOPR does not propose to abrogate pre-Order No. 888 transmission contracts.

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pricing and the elimination of pancaked rates. Accordingly, there is no requirement that the Applicants convert all existing transmission contracts to WestConnect transmission service.

120. We disagree with Tri-States' assertion that little emphasis has been placed on the preservation of existing rights. Applicants propose to mandatorily convert transmission only service between PTOs, but will maintain, through agreed upon non-converted rights instructions, existing contract service that is not converted to WestConnect transmission service. Furthermore, the voluntary nature of conversion will allow a transmission customer under a non-converted existing contract to best determine if WestConnect tariff service will better suit their transmission service requirements.

121. Consistent with our finding in RTO West⁶⁷ and Order No. 2000,⁶⁸ Applicants must make clear that transfer payments do not perpetuate pancaked charges. If a transmission customer continues to take transmission service under a non-converted existing contract and cannot reach the delivery point absent transmission service from WestConnect, the transmission customer must take additional service from WestConnect. With voluntary conversion to RTO service, a transmission customer will be able to take service under the WestConnect Tariff, but the charges for service will be based upon the rates for transmission service under the existing contract (i.e., the transfer payment).⁶⁹

2. Applicants' Proposal: Transmission Pricing

122. Applicants propose to employ license-plate transmission pricing for a transitional period that will terminate on January 1, 2009. WestConnect will use a zonal rate that uses each PTO's then-effective Tariff rate for transmission service within the WestConnect footprint. For transmission service through or out of the WestConnect grid, Applicants propose a wheeling-out rate, which will be the higher of the averaged zonal rates or the

⁶⁷See RTO West, 100 FERC at P 105.

⁶⁸See Order No. 2000 at 31,205.

⁶⁹See WestConnect Tariff, Appendix E, sections E.2.4.3.1 (Converted Type 1 and Type 2 Existing Contracts) and E.2.5.3.1 (Converted Type 4 Existing Contracts).

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zonal rate at the applicable scheduling point.⁷⁰ Applicants assert that this approach was developed to minimize cost shifting during the transition period.

123. Appendix O of the WestConnect Tariff (Transmission Service Pricing and Revenue Distribution) contains the formulas WestConnect will use to compute these zonal rates. The formulas consist of each PTO's existing annual transmission revenue requirements and a 12 coincident peak divisor. Each PTO is responsible for obtaining regulatory approval for its annual transmission revenue requirement.⁷¹ Applicants commit to making an initial rate filing with the Commission no later than 90 days before the independence date. Furthermore, section 6.2.13 of the WestConnect TCA precludes the Board from modifying Applicants' proposed pricing model and rate design without unanimous consent from the PTOs. Applicants also state that zonal rates will be billed to scheduling coordinators through an access area fee that uses a formula that tracks each scheduling coordinator's usage at the hour of the access area's monthly peak.

124. Applicants further explain that they are attempting to negotiate reciprocity agreements with adjacent RTOs and, if these negotiations are successful, inter-RTO transfer payments will replace transaction-based rates and charges for the use of an RTO's grid for inter-RTO wheeling.

125. At the end of the transitional period, Applicants propose that WestConnect will convert from zonal pricing to a "highway/zonal" approach. The highway rate will be a single system-wide, postage-stamp rate based on the combined revenue requirements for the facilities that will constitute the highway system of all transmission owners within WestConnect (i.e., the high voltage facilities that comprise WestConnect's bulk transmission grid). The zonal rate will vary based on local zones in a manner similar to that employed in developing the initial zonal rates. Zonal rates will be designed to recover annual costs of transmission facilities that provide local access within each zone, which are typically lower voltage facilities.

a. Intervenor Comments

⁷⁰Applicants define scheduling points as specific interfaces where the WestConnect grid is connected to facilities that are outside of WestConnect's operational authority. See WestConnect Tariff, Attachment 1, at 38.

⁷¹If a state regulatory authority requires the establishment of an actual dollar per-unit rate, that rate will be used in lieu of an annual transmission revenue requirements.

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126. Several intervenors argue that Applicants' proposal fails to eliminate rate pancaking. Arizona Consumer Systems states that transmission dependent utilities who own transmission facilities and take WestConnect transmission service will be required to pay both a PTO's zonal rates and all of the costs associated with the transmission facilities that the Transmission dependent utilities own that provide grid-wide support. Applicants commit to grant "consideration" for transmission facilities owned by transmission customers, but Arizona Consumer Systems asserts that the meaning of consideration is unclear. Arizona Consumer Systems suggests that credit be given to Transmission dependent utilities for transmission facilities that they either own or have a firm contract right to under their existing transmission agreements.

127. Some intervenors argue that Applicants' proposal only mitigates cost shifting between PTOs and Western. According to Navajo, Applicants have failed to adequately explain the change from the existing Order No. 888 open access transmission tariff rates to a point-to-point 12 coincident peak divisor model, the addition of grid charges, and the various rate changes to existing customers and end users.

128. The NM Attorney General favors license-plate rates and argues that New Mexico's customers will be best served by preserving the current process of state-determined cost-based (bundled) rates. Utah Municipals claims that Applicants' pricing proposal is an impermissible restraint on WestConnect's ability to set the rate level and design, and it believes that Applicants' proposal reduces WestConnect to a collection agent for PTOs.

129. Duke and EPSA argue that Applicants' pricing proposal is unjust, discriminatory, and incomplete and does not comply with Order No. 2000. In addition, Duke and EPSA argue that the disparity in price for wheeling-out service is unfair, because PTOs serving load outside WestConnect will pay their respective zonal rate, while generators will pay the higher of the wheeling-out rate or a PTO's zonal rate.

130. Tri-State asserts that WestConnect's zonal pricing proposal is unfair to utilities with geographically dispersed load and generation. Tri-State argues that PTOs serving large load centers will receive disproportionately large interests of transmission revenue, because only those PTOs with transmission facilities in the area where the load is located are compensated for a transmission transaction. Conversely, large load area customers are able to use the facilities of "transmission-rich" utilities, such as Tri-State, without compensation. Moreover, Tri-State argues that there is little opportunity for rural utilities to be compensated on a reciprocal basis by the delivery of power generated in other areas to their loads.

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131. Tri-State believes that cost shifting concerns in the West are overstated and should not bar immediate use of postage stamp rates or, at least, a transition to postage-stamp rates sooner than January 1, 2009, as proposed by Applicants. It asserts that a transition period of two or three years is more appropriate. Tri-State further argues that although zonal pricing and network pricing appear similar, the application of an access area rate to a network customer can increase the customer's monthly transmission bill. Tri-State asserts that present-day network service is billed based on the customer's load ratio share. Under the zonal rate methodology, each month a customer will pay the zonal rate multiplied by its load on the hour of the zone's monthly peak hour. Thus, under the network pricing method, network customers are paying for their actual use of the system. However, under Applicants' proposal, network service customers will always pay a fixed share of a transmission provider's revenue requirement due to the fixed point-to-point transmission rate they pay for monthly service.

132. Arizona Consumer Systems asserts that the criteria for the creation of a zone set forth in Appendix O of the WestConnect Tariff are unjust, unreasonable, and unduly discriminatory, because they prevent smaller but substantial transmission-owning entities from becoming access areas. Consequently, the proposal results in an anti-competitive allocation of the transmission market among the existing PTOs.⁷²

b. Applicants' Response

133. Applicants state that the zonal rate structure mitigates the risks that were recognized by the Commission in Order No. 2000. Applicants state that Order No. 2000 allows for various RTO proposals regarding the allocation of fixed transmission cost recovery, including using license-plate rates so that cost shifting does not impede RTO formation. They state that their pricing proposal is consistent with other orders already issued by the Commission.⁷³

⁷²Arizona Consumer Systems opposes the requirements that a PTO have: (1) a minimum original cost of pricing authority facilities of \$25,000,000; (2) a minimum of one hundred circuit miles of transmission lines rated at 115 kV or above; and (3) a minimum effective transmission rate of \$1.00/kW-month.

⁷³See, e.g., GridFlorida, LLC, 94 FERC ¶ 61,363 at 62,346-48 (2001) (GridFlorida II); Alliance Companies, 96 FERC ¶ 61,052 at 61,132 (2001); PJM Interconnection, *et al.*, 81 FERC ¶ 61,257 at 62,249 (1997); Midwest Independent Transmission System Operator, Inc., 84 FERC ¶ 61,231 at 62,151 (1998).

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134. In support of their license-plate proposal, Applicants argue that transmission-owning entities in the Southwest have transmission rates that differ by a ratio of as much as four to one. To encourage the participation of a diverse cross-section of entities, the support of the state Commissions, and support of the boards of non-jurisdictional entities, cost shifting must be eliminated and customer transmission costs must be minimized. Applicants state that if the Commission were to retreat from its record of supporting license-plate pricing for RTOs, it will be harmful to the goal of achieving a workable RTO structure in the Southwest.

135. Applicants clarify that there may be instances where transmission customers with existing contracts over multiple PTOs' systems will pay both the existing contract charge and the zonal rate for PTOs. However, Applicants explain that existing contracts with PTOs, which are needed to facilitate the complete delivery to specific load or loads, could have been entered into under separate contracts with those PTOs. If some of these contracts terminate, while others do not, the transmission customer must take service under the existing contract as well as taking transmission service from WestConnect. Applicants also clarify that PTOs will pay the appropriate wheeling-out rate.⁷⁴

136. Applicants state that their long-term pricing proposal is conceptual in nature and note that the final decision as to what will be filed with the Commission has been assigned to the Board. Applicants argue that the intervenors misrepresent Applicants' proposal when they claim that it does not contemplate or commit to a long-term pricing structure and that the intervenors ignore the merits of the highway/zonal approach in Appendix O of the WestConnect Tariff.⁷⁵ Applicants address the intervenors' specific rate concerns by reiterating that they have not sought Commission approval of specific rates but, instead, general guidance from the Commission on their proposed methodology.

c. Discussion

137. Applicants state that they are not seeking regulatory approval of rates; they are merely requesting general guidance from the Commission. Thus, we are not making a determination on the justness and reasonableness of the zonal rate and the access area fee

⁷⁴See Applicants' Answer at 32.

⁷⁵Applicants anticipate making their first filing regarding long-term pricing structure some time in 2002. See WestConnect Tariff, Appendix O, Section O.9.1 (d) (General Provisions).

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formulas, including the use of the 12 coincident peak divisor employed therein. Applicants are required to file for the Commission's approval of these formulas and the ultimate rates in a section 205 rate filing.

138. In Order No. 2000, the Commission stated:

It is appropriate to allow RTOs to propose the use of license plate rates for a fixed term of the RTO's choosing. However, RTOs that propose the use of license plate rates must make clear how transmission expansion will be priced, that is, whether license plate rates or some other mechanism will be applied to the cost of new transmission facilities, and how such pricing affects incentives for efficient expansion. In addition, we will require that before the end of the fixed term, the RTO must complete an evaluation of fixed cost recovery policies based on the factual situation of the particular RTO, and file with the Commission its recommendations on any changes that should be instituted.⁷⁶

139. Applicants' proposal to retain license plate rates for an interim period and then to adopt a combined system-wide postage stamp/zonal pricing scheme is consistent with Order No. 2000.⁷⁷ The duration of the proposed transition period is intended to foster participation in WestConnect by market participants, including public power entities. While the Standard Market Design NOPR contemplates a shorter transition period for conversion to service from an independent transmission provider under a single rate design,⁷⁸ we understand Applicants' concern for certainty with respect to potential cost shifts.

140. We do not agree with Arizona Consumer Systems that transmission dependent utilities that take transmission service from WestConnect will incur pancaked rates. Applicants propose to allow transmission credits for transmission dependent utilities upon a showing that a transmission dependent utilities' facilities are integrated into the planning

⁷⁶Order No. 2000 at 31,177.

⁷⁷See id.

⁷⁸See Standard Market Design NOPR at PP 167-178.

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and operation of the WestConnect grid and provide a benefit to that grid.⁷⁹ In order to facilitate one-stop shopping, as envisioned by Order No. 2000, WestConnect, as the transmission provider, must either provide the transmission credits or the methodology by which the credits will be determined and allocated for non-RTO facilities used by WestConnect in providing services. We require Applicants to modify their proposal to reflect this.

141. Applicants' proposal to assess the wheeling-out rate is reasonable as a transitional pricing mechanism. Absent the imposition of an export fee or some other mechanism to recover the cost of transmission, customers outside the WestConnect footprint will not contribute to the recovery of the cost of the transmission system. However, we agree with Duke and EPSA that the proposal gives an undue pricing preference to PTOs. Section O.5.2.3 of Appendix O states that transmission service for a PTO to resident load that is outside of WestConnect will only be charged the zonal rate of that PTO's zone and will not be considered wheeling out for purposes of transmission service.⁸⁰ We find that this proposal is unduly preferential to the PTOs and, therefore, is unjust and unreasonable; PTOs and generators must be assessed the same price for wheeling-out service.

142. As noted by the Applicants, they and other entities in the West have formed an organization, the Steering Group, that is exploring, among other things, price reciprocity between RTOs in the West.⁸¹ We look to Applicants to continue their efforts to address

⁷⁹We note that the Standard Market Design NOPR proposes that the seven factor test be used to determine which facilities belong under the control of an independent transmission provider. See id. at P 367. This proposed test focuses on the presumption that if a facility is transmission, it belongs under the control of the independent transmission provider; thus, once a determination is made with the seven factor test, there would be no need for an additional review under the Commission's previous integrated facilities test. See id. at P 368.

⁸⁰Applicants define resident load, in relevant part, as load outside the WestConnect control area for which a PTO has an obligation to serve.

⁸¹See RTO West at P 136 (noting that applicants and other entities throughout the West have formed an organization that is exploring, among other things, price reciprocity between RTOs in the West and stating that we look to applicants to continue their efforts to address this issue through the Steering Group, with the goal of assigning the costs of

(continued...)

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this issue through the Steering Group, with the goal of assigning the costs of transmission to load regardless of its location rather than to the supplier of the energy.

3. Applicants' Proposal: Grid Charge

143. The WestConnect Tariff contains a grid charge comprised of two components: (1) a grid management component; and (2) a transmission adjustment component. The grid management component is intended to cover all the costs of operating the grid and administering the WestConnect Tariff that are not recovered through scheduling and dispatch service and may include start-up costs, including costs associated with DesertSTAR and other charges and credits that cannot be identified and assigned to a specific scheduling coordinator. Applicants state that a rate-of-return component will also be included where appropriate (*i.e.*, the grid management component may include certain financing costs). The grid management component will be applied to all scheduling coordinators with loads and those performing wheeling-out transactions.

144. The transmission adjustment component will be applied to all scheduling coordinators and is intended to provide compensation to Western for revenues lost under the initial pricing structure. According to Applicants, the transmission adjustment component addresses Western's loss of revenues associated with non-firm and short-term firm transmission sales and contracts with entities that serve load in other access areas. These revenues will terminate as a result of Western's conversion to WestConnect service. Applicants state that this charge is similar to that included for the New York Power Authority under the New York ISO's Tariff.⁸² Applicants ask the Commission to approve the grid charge, subject to review of the actual costs, which will be submitted no later than 90 days before operations commence.

a. Intervenor Comments

145. Arizona Consumer Systems contend that loads not located in Western's zone that purchase power and energy from generators connected to Western's transmission facilities will be required to pay several sets of pancaked rates. According to Arizona Consumer Systems, these loads will pay both Western's transmission charge allocated to generators

⁸¹(...continued)

transmission to load regardless of its location rather than to the supplier of the energy).

⁸²See Transmittal Letter at 25.

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and the PTO's zonal rate, which will include another component of compensation for Western (i.e., the transmission adjustment component). Applicants should either provide a credit for transmission charges assigned to generators on Western's system or require the members of Arizona Consumer Systems to assign comparable transmission charges to generators connected to their transmission systems. Arizona Consumer Systems states that this adjustment will alleviate the multiple transmission charges to customers purchasing power and energy from generation located on Western's transmission system.

b. Applicants' Response

146. Applicants do not address specific concerns regarding the grid charge but, instead, suggest that the comments pertaining to these issues are premature, given the nature of Applicants' petition.

c. Discussion

147. The use of a grid charge to recover the costs of WestConnect's operations is appropriate. Applicants propose a formula that will compute a dollar-per-kilowatt-hour rate. As with the formula rates used to determine their transmission service charges, we find that the concept of a formula for determining the grid charge is reasonable, but require that WestConnect make a filing under section 205 of the FPA for approval of this formula as the rate. Critical details (such as how often the rate will be updated, the level of the return component, if any, and other costs) are not identified. In order to determine the output of the formula and that the formula itself is just and reasonable, Applicants must make a detailed section 205 filing. At that time, Arizona Consumer Systems should raise their issues regarding credits.

148. Applicants' proposed transmission adjustment component encourages Western's participation in WestConnect by ensuring that its embedded costs will be recovered without major cost shifts. Western provides preference power to load serving entities throughout the Western interconnection, many of which will not be in the WestConnect footprint. Load that currently pays a significant portion of Western's transmission revenue requirement will be located outside of the proposed WestConnect system. As such, with the use of license plate pricing during the transition period, these off-system loads will no longer be required to pay for the use of Western's transmission assets. Furthermore, Western utilizes a great deal of short-term and non-firm transmission service to other systems located within the WestConnect system. Accordingly, Western faces potential cost shifts absent a mechanism that will provide for those lost transactions.

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Accordingly, we accept the transmission adjustment component for the transition period; however, the transmission adjustment component must only be used to compensate Western for its lost revenues if it participates in WestConnect.

4. Applicants' Proposal: Interconnection Service Requests

149. WestConnect will be responsible for providing interconnection service to all grid facilities and shall: (1) receive and process all requests for interconnecting new facilities or modifying existing facilities; (2) process and execute interconnection study agreements; and (3) ensure that interconnections to grid facilities owned by PTOs are completed in a timely manner. An interconnection agreement is not required when a PTO proposes to interconnect new generation to or modify existing interconnections on its own facilities.

150. The WestConnect Tariff requires that WestConnect consult with PTOs to: (1) define technical interconnection standards; (2) define the scope, methodologies, and assumptions used in each interconnection study; (3) perform or out-source to other entities (including the affected PTOs) interconnection studies pursuant to WestConnect's policies and procedures; and (4) sign interconnection agreements.

151. Applicants state that WestConnect, in conjunction with PTOs, will develop interconnection standards within one year after the independence date that are consistent with the interconnection principles and requirements of the Western Electric Coordinating Council and the North American Electric Reliability Council for the design, construction, inspection, and testing of proposed interconnections in the WestConnect region. Applicants state that these standards may vary to reflect the historical practices and technical standards of each individual PTO, provided that such standards are reasonable, non-discriminatory, and not preferential to the commercial interests of any market participant.

152. Each PTO will have the right of first refusal to own interconnection facilities that connect to its system, and the costs of such facilities will be recovered through the PTO's zonal rate. If a PTO opts not to own the facilities, WestConnect shall have the right of first refusal and customers shall be billed through the grid charge. If neither WestConnect nor a PTO assumes ownership of the facilities, a third party may assume ownership under the same terms and conditions. If a third party sponsors an interconnection project, the affected PTO has the right to assume ownership of the facilities and to reimburse the third party by making payments amortized over the book life of such facilities. If WestConnect assumes ownership, it will grant credits to the affected party in accordance with the Commission's policy.

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a. Intervenor Comments

153. Some intervenors argue that providing transmission credits to interconnection customers only for WestConnect-owned facilities violates the Commission's policy that "all Network Upgrade costs (the cost of all facilities from the point where the generator connects to the grid), including those necessary to remedy short-circuit and stability problems, should be credited back to the customer that funded the upgrades once delivery service begins."⁸³ Other intervenors request clarification of which facilities will receive transmission credits under section 10(C) of Appendix Q of the WestConnect Tariff.

154. Intervenor state that the Commission has emphasized that independence is compromised when transmission owners are overly involved in the interconnection process. Accordingly, intervenors ask the Commission to grant WestConnect the authority given to PTOs under Appendix Q of the WestConnect Tariff and to direct Applicants to remove the provisions that require WestConnect to consult with PTOs.

155. In addition, certain intervenors take issue with the distinction between PTO and WestConnect ownership of interconnection facilities, regarding the application of transmission credits for network upgrades as a result of the interconnection request. They argue that a PTO should not be permitted to amortize credits when the initial payments for such facilities were not amortized. These intervenors also disagree with a PTO's right under Applicants' proposal to acquire valuable projects for itself that were proposed and paid for by third parties.

156. Many of the intervenors believe that the Commission should defer ruling on the proposed interconnection procedures until the conclusion of the Commission's rulemakings on standardizing interconnection processes.⁸⁴

⁸³Consumers Energy Company, 95 FERC ¶ 61,233, reh'g denied, 96 FERC ¶ 61,322 (2001).

⁸⁴See Standard Generator Interconnection Agreements and Procedures, ___ Fed. Reg. ___ (2001), FERC Stats. & Regs. ¶ 35,540 (2001), Notice of Proposed Rulemaking; see also Standardization of Small Generator Interconnection Agreements and Procedures, ___ Fed. Reg. ___ (2001), FERC Stats. & Regs. ¶ 35,540 (2001), Notice of Proposed Rulemaking (collectively, Generator Interconnection NOPR).

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b. Applicants' Response

157. Applicants ask that the Commission not defer ruling on this matter, as requested by some of the intervenors. With respect to the intervenors' claim that PTOs are overly involved in the interconnection process, Applicants assert that if, at some future date, the PTOs transfer full ownership of their transmission systems to WestConnect, then WestConnect alone may coordinate with the interconnecting entity. However, until that time, PTOs believe that they must be involved in this process because of the significant portion of the transmission system that certain PTOs own jointly with entities that do not plan to participate in WestConnect. In addition, PTOs argue that they must retain ownership of their facilities to protect their investments, to prevent liability concerns, and to reliably serve their native loads under state law. Moreover, Applicants contend that exclusion from the interconnection process is not an option for non-jurisdictional entities with certain tax situations or RUS involvement.

c. Discussion

158. We find that the proposed interconnection process, with modification, will meet the requirements of Order No. 2000. WestConnect will process all requests for interconnection to the facilities comprising the WestConnect grid, execute interconnection study agreements, and set forth procedures for interconnection queue priority.

159. We believe Applicants' proposal to allow PTOs to have the right of first refusal to own interconnection projects proposed by third parties has not to date been explained or justified, and we direct Applicants to explain why such a proposal is necessary.

160. We require that all WestConnect's interconnecting transmission customers sign interconnection agreements. Applicants' proposal allows a PTO that proposes to interconnect its own new generation or modify interconnections to upgrade its own facilities to avoid entering into an interconnection agreement with WestConnect. This proposal is unduly discriminatory; it will allow the PTO to avoid the interconnection queue process and allow the PTO to construct an interconnection pursuant to standards inconsistent with WestConnect. Accordingly, this provision is rejected.

161. Contrary to intervenors' arguments, we find that the participation of PTOs in the development of interconnection standards can be valuable; PTOs are in a better position to determine near-term facility ratings, capabilities, and design and can provide valuable assistance in the collection of information in the interconnection study process. However,

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PTOs are not allowed to participate in the process of deciding on particular interconnection requests; that is WestConnect's responsibility.

162. We note that many issues regarding the interconnection process are being addressed by the Commission in the Generator Interconnection NOPR.⁸⁵ Therefore, we remind Applicants that the interconnection proposal, as accepted herein, will be subject to the outcome of those rulemakings. As such, the issues that intervenors raise regarding credits for network upgrades will be resolved by the Generator Interconnection NOPR.

H. RTO Function No. 2: Congestion Management

The RTO must ensure the development and operation of market mechanisms to manage transmission congestion. The RTO must satisfy the market mechanism requirement no later than one year after it begins to operate. However, it must have in place at the time of initial operation an effective protocol for managing congestion.

1. Applicants' Proposal: Physical Rights Congestion Model

163. Applicants propose a zone-based approach to manage congestion on the WestConnect grid. Specific transmission rights will not be needed to schedule transmission service within a congestion zone.⁸⁶ However, for transmission service between congestion zones within the WestConnect grid or over scheduling points to exit the grid, a customer must acquire transmission rights to schedule service.⁸⁷

⁸⁵See id.

⁸⁶Applicants define congestion zone as "a portion of the WestConnect grid where the costs of managing congestion are expected to be commercially insignificant." See WestConnect Tariff, Attachment 1, at 11.

⁸⁷Transfer points between congestion zones are known as FTR interfaces, which are lines or groups of lines. A scheduling point is a location at which the WestConnect grid is connected to transmission facilities that are outside WestConnect's operational authority and includes points internal to the WestConnect footprint where its facilities connect to those of a non-participating transmission owner.

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164. WestConnect will provide physical transmission rights over specific contract paths within the WestConnect footprint in the following tradeable forms: (1) firm transmission rights (FTRs); (2) recallable physical transmission rights (recallable rights);⁸⁸ and (3) non-firm transmission rights. WestConnect will also issue non-converted transmission rights to accommodate existing contract holders. Applicants state that the quantity of transmission rights required for each FTR interface or scheduling point shall be determined by WestConnect, as specified in the FTR requirements matrix,⁸⁹ and posted on WestConnect's website at least six months prior to the independence date. A change to an FTR interface or scheduling point must be preceded by Board action at least 90 calendar days before the proposed effective date.

165. All FTRs will be initially auctioned.⁹⁰ FTRs may be offered in annual, monthly, bi-monthly, and daily blocks. The amount of FTRs to be auctioned will be based on the operating transfer capability of the FTR interface and scheduling point (including added operating transfer capability resulting from the use of phase shifters), notwithstanding any transfer capability reserved for existing non-converted rights contracts. If PTOs are willing to bid the maximum price (\$9,999.99/MW), PTOs will have priority over other bidders to receive FTR allocations for priority service to bundled native load and wholesale requirements customers. This cost of redispatch will be charged to all scheduling coordinators with load within the congestion zones.

166. Applicants state that the day-ahead scheduling and settlement process will be the primary instrument for scheduling all uses of the WestConnect grid (e.g., energy, transmission rights, and ancillary services). During the day-ahead process, WestConnect also proposes to administer a balancing market. Upon completion of the day-ahead scheduling process, WestConnect will commence its schedule adjustment process, which will end 60 minutes before the trading day. During the schedule adjustment process, WestConnect will evaluate the impact of various schedule change requests to ensure that the proposed changes will neither increase intra-zonal congestion nor create grid security

⁸⁸Recallable rights result from the non-use of FTRs and the non-use of non-converted physical scheduling rights associated with existing contracts that have not been converted to service under the WestConnect Tariff.

⁸⁹Applicants describe the matrix as a tool by which WestConnect will determine the usage of each scheduling coordinator at an FTR interface or scheduling point.

⁹⁰Each FTR represents the right to transfer one MW of energy or ancillary services in a specific direction across an FTR interface or scheduling point for one hour.

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problems.⁹¹ In addition, during the schedule adjustment process, recallable rights will become firm rights (i.e., they are no longer subject to recall).

167. When inter-zonal congestion (i.e., congestion on FTR interfaces and scheduling points) occurs and WestConnect determines that there is insufficient time to institute and schedule curtailments of transmission rights, WestConnect may order, in accordance with Appendix C of the WestConnect Tariff (Dispatch and Emergency Operations), the redispatch of energy and capacity based on the bids that scheduling coordinators have submitted in the balancing energy stack.⁹² This process will take place one hour before each settlement period of the trading day.⁹³ If the bids in the balancing energy stack are insufficient to relieve the constraint, WestConnect may issue instructions for redispatch of any resources, but only to the extent necessary to relieve the congestion and for the time it takes WestConnect to implement schedule curtailments under Appendix A of the WestConnect Tariff (Congestion Management).

168. Applicants state that when intra-zonal congestion (i.e., congestion within a congestion zone) is identified, WestConnect will first attempt to eliminate it by using the voluntary congestion redispatch bids submitted to WestConnect in the day-ahead scheduling process. If congestion is not eliminated, WestConnect may exercise its authority to reschedule bids submitted by scheduling coordinators. These redispatch costs will be charged to all scheduling coordinators with load within the congestion zone.

⁹¹WestConnect states that it may accept a proposed schedule change that causes intra-zonal congestion, but only if there are sufficient congestion redispatch bids available in the relevant location to eliminate congestion.

⁹²Applicants state that WestConnect will develop and update a balancing energy stack, which will be used to: (1) ensure that loads are balanced; (2) respond to contingencies; (3) mitigate inter-zonal and intra-zonal congestion; (4) maintain voltage levels throughout the WestConnect grid; (5) enable resources providing regulation service to return to their preferred operating points; and (6) enable the return to reserve status of spinning reserves and non-spinning reserves that are called upon during the settlement period.

⁹³Supplemental energy resources may be submitted thirty minutes before the start of the settlement period and withdrawn at any time before the issuance of a dispatch instruction to the offered supplemental energy resource.

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169. Applicants believe that by using a physical rights model, the cost of transmission service can be determined in advance of use and thereby can provide clear price signals to the market. Unlike in the Eastern Interconnection, Applicants assert that in the West there are rarely alternate paths between a generator and load and therefore many transmission paths in the West are frequently constrained. According to Applicants, the physical rights model has proven to be effective at managing congestion in the Southwest, and stakeholders, especially non-jurisdictional entities, who participated in developing an RTO in the Southwest strongly favor this model.

a. Intervenor Comments

170. EPSA claims that the process for mandatory rescheduling for congestion redispatch service, are confusing and therefore requests that the Commission clarify that generators subject to mandatory rescheduling must receive compensation for costs incurred, including lost opportunity costs. EPSA further argues that WestConnect's physical rights congestion model guarantees PTOs a competitive advantage. For instance, Appendix A of the WestConnect Tariff allows PTOs priority over other bidders for receiving FTR allocations in the auction of these rights, while providing no justification for this preference. In addition, EPSA notes that because existing contracts are excluded from the WestConnect Tariff, there will be less operating transfer capability, which effectively reduces the available FTRs. EPSA argues that existing contracts should be placed under the WestConnect Tariff, including the congestion management proposal.

b. Applicants' Response

171. Applicants claim that PTOs should have priority rights for access to congested facilities in order to prevent their retail customers from being injured economically by the formation of WestConnect. Applicants argue that section 9.2 of Appendix A of the WestConnect Tariff does not give PTOs any higher priority than scheduling coordinators that serve FTR requirements loads. Applicants note that the Commission has recognized that states have jurisdiction over bundled retail load and argue that the Commission should accommodate efforts to respect jurisdictional boundaries and balance competing interests.

c. Discussion

172. Applicants' congestion management proposal requires the use of redispatch and curtailment to relieve congestion. Although Order No. 2000 provides that physical tools are acceptable at commencement of RTO operation; it envisions that the congestion

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management program ultimately implemented by an RTO will use market-driven mechanisms to clear congestion. Consequently, we will approve Applicants' congestion management proposal as a "Day One" mechanism and, as discussed below, direct Applicants to engage in further discussions to develop a congestion management program that reflects market-driven solutions to clear congestion.

173. We are concerned about the use of congestion zones in Applicants' proposal. The Commission acknowledges that the theory of the zonal method is that zones can be established within which little transmission congestion will occur (*i.e.*, if any congestion does occur within a zone, then all customers receiving power within the zone must share the cost of congestion). Variants of zonal pricing were tried in California, PJM, Texas, and New England.⁹⁴ In these cases, the methods contained a similar flaw: the use of the zonal price signal was not assigned directly to the transactions causing the congestion including transactions with loop flow over the constrained path. For example, during the first year of its ISO operations, PJM operated as a single zone for purposes of congestion management; energy prices did not vary by location to reflect transmission congestion within PJM. As a result of the failure to adequately price congestion, customers increased their self-schedules of energy over congested paths, thereby further increasing congestion, causing unnecessary costs and a loss of reliability. In California, the zonal congestion management system encouraged market participants to create inefficient intra-zonal congestion by overscheduling energy flows on congested intra-zonal transmission paths in the day ahead schedule; and then profit from relieving the artificial congestion in real time.

174. In GridSouth II,⁹⁵ the Commission ordered the RTO not only to develop a market-based proposal for managing congestion, but to consider congestion management mechanisms employed by other grid operators in the industry.⁹⁶ The Commission directed GridSouth to either implement the best practices from among the mechanisms currently in

⁹⁴See New England Power Pool, 88 FERC ¶ 61,147 (1999); PJM Interconnection, LLC, 81 FERC ¶ 61,257 (1997), order on reh'g, 92 FERC ¶ 61,282 (2000); Order Proposing Remedies for California Wholesale Electric Markets, 93 FERC ¶ 61,121 (2000).

⁹⁵See GridSouth Transco, LLC, et al., 96 FERC ¶ 61,067 (2001) (GridSouth II).

⁹⁶See id. at 61,299.

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use by other grid operators or explain why its proposal was superior to the industry's existing best practices.⁹⁷

175. The California ISO and the filing utilities of RTO West have both proposed a locational pricing model that uses financial transmission rights for managing congestion within their respective regions. We believe that in order to provide service over as large an area as possible and reduce seams issues between RTOs in the West, Applicants' congestion management proposal must be compatible with the other congestion management models being developed in the West. Therefore, we require WestConnect to develop a congestion model that does not artificially create seams among the Western RTOs. We also require Applicants to use the Steering Group as a vehicle to ensure the proposals of RTO West, California ISO, and WestConnect are compatible.

176. In order that the requirements for establishing a market-based congestion management system are fully understood and appropriately incorporated into the structure of WestConnect operations, we direct Applicants to hold discussions among stakeholders and staff to hold technical conferences to facilitate further development of WestConnect's congestion management proposal.

I. RTO Function No. 3: Parallel Path Flows

An RTO should develop and implement procedures to address parallel path flow issues within its region and with other regions.

1. Applicants' Proposal

177. Applicants state that parallel path flows within the WestConnect region will be mitigated through the congestion management system in the WestConnect Tariff. Applicants explain that major loop flows within the Western interconnection are currently managed through the use of the Commission-approved Western Electric Coordinating Council unscheduled flow mitigation plan, which uses phase shifting transformers throughout the Western interconnection. Applicants claim that the unscheduled flow mitigation plan is an integral part of the WestConnect Tariff and, together with WestConnect's congestion management plan, will address any parallel path flows.

⁹⁷See id.

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a. Discussion

178. We conclude that continued use of the unscheduled flow mitigation plan meets the minimum requirements of this function. To date, the unscheduled flow mitigation plan has not been amended to accommodate RTOs; however, Applicants, in their July 3 clarification, note that the Steering Group has indicated that this issue has been resolved. We will review any additional procedures for mitigating loop flows when revised procedures are filed with the Commission by Applicants that reflect the resolutions developed through the Steering Group. This is consistent with the requirement we have established in RTO West.⁹⁸

J. RTO Function No. 4: Ancillary Services

The RTO must serve as a provider of last resort for all ancillary services required by Order No. 888 and subsequent orders.

1. Applicants' Proposal: Market Approach for Ancillary Services and Non-Market Ancillary Services

179. Applicants propose to establish a market approach for obtaining the following ancillary services: regulation service; load-following-up service; load-following-down service; spinning reserve service; non-spinning reserve service; and supplemental energy service. Scheduling coordinators under the WestConnect Tariff may self-supply these services or use WestConnect as the provider of last resort. WestConnect will also be the provider of: balancing energy service; voltage support service; scheduling and dispatch service; black start service; congestion redispatch service; and local generation resource service. A market approach will also be used for balancing energy service and local generation resource service.

180. Based on the day-ahead scheduling process, WestConnect will determine the daily requirements for regulation, load following, and operating reserves to be procured in the market. Scheduling coordinators with qualified resources may submit bids to provide these services as part of the day-ahead scheduling process. The market clearing price for each service will be equal to the highest priced capacity reservation bid accepted by WestConnect for providing that ancillary service. If WestConnect must procure these

⁹⁸See 100 FERC at P 177.

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ancillary services on a location-specific basis due to congestion, WestConnect will determine a market clearing price for each congestion zone.

181. WestConnect will use the market based ancillary service bids and energy price curve data that will be submitted by the scheduling coordinators to create a balancing energy price stack through which available resources will be economically dispatched to meet real-time balancing energy needs. The balancing energy price stack may be updated by WestConnect with supplemental energy bids submitted by scheduling coordinators. Transmission customers' charges for balancing energy service will be calculated in ten-minute increments.

182. WestConnect will manage load pocket conditions by providing local generation resource service.⁹⁹ When load pocket conditions are identified in the day-ahead scheduling, generating units with local generation resource obligations must submit, in an auction process, all unscheduled energy. The local generation resource service will be monitored by the WestConnect market monitor, who will provide progress reports to the Board and the Commission on the performance of the local generation resource service. The progress reports will be submitted on each anniversary of the day on which WestConnect commences operations.

183. WestConnect will offer congestion redispatch service through which scheduling coordinators, or other owners of generation, will contractually commit to WestConnect the ability to change scheduled output or consumption levels of generating units and dispatchable demands through the use of congestion redispatch bids. WestConnect will contract with generating units through a competitive procurement process in order to provide long-term voltage support and black start capability. Scheduling and dispatch service will be provided directly by WestConnect.¹⁰⁰

⁹⁹Load pocket conditions, according to Applicants, occur when forecasted demand in a load pocket exceeds the sum of the forecasted import capability into a load pocket and the forecasted committed output of resources within the load pocket. See WestConnect Tariff, Attachment 1, at 26.

¹⁰⁰Applicants define congestion redispatch as the means by which WestConnect will manage intra-zonal congestion. See WestConnect Tariff, Appendix D.2.11 (Congestion Redispatch Service).

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a. Intervenor Comments

184. Arizona Consumer Systems and the NM Attorney General claim that Applicants' proposal for ancillary services fails to meet the requirement of Order No. 2000 for ancillary service because it does not create competitive ancillary service markets. The NM Attorney General stresses the need for an energy balancing mechanism based on actual costs, rather than bids, until WestConnect develops operational experience. In addition, the NM Attorney General believes that various charges (e.g., transmission adjustment component, revenues for ancillary services, and the grid charge) should be capped at their current cost-based levels.

185. Duke states that Applicants' proposal for local generation resources should be rejected because it does not allow for a competitive market for ancillary services in congestion zones where the local generation resources are offering service to determine the clearing price. Therefore, Duke believes that Applicants' proposal will discourage investment in load pocket areas.

b. Discussion

186. We find that the concept of Applicants' proposal for ancillary services conforms to the requirement of Order No. 2000, because it will facilitate a competitive market for ancillary services. In addition, we find that Applicants' proposal to develop and operate a real-time balancing market is consistent with Order No. 2000; therefore, we accept it.¹⁰¹ The Commission finds the development of a competitive ancillary services market and access to a real-time balancing energy mechanism will promote efficient pricing. Accordingly, we will not require the ancillary services proposal be modified to establish cost-based rates for the energy balancing and other ancillary services charges. In order to facilitate a competitive ancillary services market, sellers and buyers must be allowed to respond based upon supply and demand signals.

187. Applicants' proposal requires that PTOs, as well as other market participants, have market-based authority for providing ancillary services under the WestConnect Tariff.

¹⁰¹See Order No. 2000 at 31,141.

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Therefore, WestConnect will be required to support its market approach in a future filing.¹⁰²

188. We disagree with Duke's argument that Applicants' proposal for local generation resource service will discourage investment. proposal provides compensation to generating units in load pockets, which must bid all unscheduled energy to WestConnect, will be based on the greater of the balancing energy clearing price in the congestion zone adjacent to the load pocket or the lesser of the generator's demonstrated cost and its bid price for local generation resource energy. This feature of the proposal would appear to encourage generation investment in the load pocket. This is further supported by Applicants' definition of "demonstrable costs" to include all costs, including variable production costs.¹⁰³ While this proposal attempts to mitigate market power that local generation resources may have in a load pocket situation by using the market price of balancing energy in the area surrounding the load pocket, it should not discourage investment in load pockets.¹⁰⁴ However, we expect, as detailed in Appendix D of the WestConnect Tariff, that WestConnect and an independent market monitor will review the performance of the local generation resource service to make sure that it allows for the operation of a competitive market for ancillary services in congestion zones.¹⁰⁵

K. RTO Function No. 5: OASIS, TTC, and ATC

The RTO must be the single OASIS site administrator for all transmission facilities under its control and must independently calculate TTC and ATC.

1. Applicants' Proposal

¹⁰²Applicants have committed to a future filing, subject to the outcome of their petition for declaratory order.

¹⁰³See Applicants master definitions list at 14.

¹⁰⁴The Standard Market Design NOPR proposes to impose a resource adequacy requirement on load serving entities. This requirement could create incentives to locate generation in load pockets.

¹⁰⁵See, e.g., Section D.9.10(e) of Appendix D.

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189. Applicants state that WestConnect will be the single OASIS site administrator for all transmission facilities under its operational authority.¹⁰⁶ They explain that within the Western interconnection, the concept of operating transfer capability (which reflects the seasonal capacity of congested interfaces and of interconnections to non-WestConnect control areas) is similar to total transmission capability. Accordingly, Applicants state that WestConnect will be responsible for the determination of operating transfer capability, total transmission capability, and available transmission capacity,¹⁰⁷ and each PTO will provide WestConnect with the data necessary for WestConnect to calculate them. If a dispute arises with respect to WestConnect's calculations, WestConnect's operating transfer capability, total transmission capability, and available transmission capacity determinations shall be the applicable calculations, pending final resolution through the WestConnect ADR process and the appeals process at the Commission.

a. Intervenor Comments

190. Some intervenors assert that the participation of PTOs in the total transmission capability and available transmission capacity calculation process will compromise the independent decision-making of the Board.¹⁰⁸

b. Discussion

191. Order No. 2000 states that an RTO must be the single OASIS site administrator for all transmission facilities under its control, must independently calculate available transmission capacity and total transmission capability and must base the calculation of available transmission capability values on data developed partially or totally by the

¹⁰⁶See WestConnect Tariff, Appendix I (WestConnect Website).

¹⁰⁷Applicants propose that WestConnect develop protocols that include the criteria and calculation methodologies for operating transfer capability, total transmission capability, and available transmission capacity, based on the Western Electric Coordinating Council's criteria. However, the Western Electric Coordinating Council's criteria may be subject to interpretation by WestConnect in developing the protocols. See WestConnect Tariff, Appendix A, Section 7.1.

¹⁰⁸See, e.g., US Executive Agency, Tractebel, EPSA, Duke, and Constellation.

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RTO.¹⁰⁹ We preliminarily find that WestConnect will satisfy the requirements of this RTO function because WestConnect will determine operating transfer capability, total transmission capability, and available transmission capability and, if a dispute arises, its determination will prevail pending resolution through the WestConnect ADR process or by this Commission. However, Applicants have not provided details concerning the criteria and calculations that WestConnect will use to determine operating transfer capability, total transmission capability, and available transmission capability values.¹¹⁰ Therefore, our finding that WestConnect will meet the requirements of Order No. 2000 for this function is preliminary, and we cannot make a formal determination until these details are filed with us and found to be just and reasonable.

192. With respect to the arguments raised by intervenors that participation by PTOs in the available transmission capability calculation process will impair the Board's independence, we find that PTOs will merely provide the necessary data for WestConnect to calculate total transmission capability and available transmission capability values and that such involvement is acceptable so long as the data is independently verified by WestConnect.¹¹¹ Applicants commit that WestConnect will be responsible for the oversight and confirmation of any studies performed by any PTO on WestConnect's behalf. Participation by PTOs in the data collection process can be vital; PTOs are in a better position to determine near-term facility ratings and capabilities and can provide valuable assistance in the collection and clarification of such data. Accordingly, we find that PTOs will not have the ability to impair the independent decision-making of the Board.

L. RTO Function No. 6: Market Monitoring

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 to propose appropriate actions for addressing them.

¹⁰⁹See Order No. 2000 at 31,145.

¹¹⁰See, e.g., WestConnect Tariff, Appendix A, Section 7.1.

¹¹¹See, e.g., *Midwest Independent System Operator, Inc., et al.*, 84 FERC ¶ 61,231 at 62,154, order on reconsideration, 85 FERC ¶ 61,250, order on reh'g, 85 FERC 61,372 (1998); *Midwest Independent Transmission System Operator, Inc.*, 97 FERC ¶ 61,326 at 62,516 (2001).

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1. Applicants' Proposal

193. Applicants propose that WestConnect establish a Market Monitoring Unit and that an outside independent market advisor may be retained by the Board.¹¹² The Market Monitoring Unit will be subject to oversight by the CEO of WestConnect, and the compensation of the head of the Market Monitoring Unit shall be determined by the Board. The Market Monitoring Unit will have its own budget for staffing and resources, which shall be approved by the Board. Applicants propose that the head of the Market Monitoring Unit report directly to the Board.

194. The Market Monitoring Unit's functions include: (i) identifying abuses of market power and undue discrimination in WestConnect's markets; (ii) monitoring compliance with WestConnect's standards, practices, and rules, as established in the WestConnect Tariff; (iii) determining opportunities for improvements in the service markets; (iv) collecting information and preparing reports, which are subject to review and comment, for the Board, Stakeholder Advisory Committee, market participants, and governmental authorities; and (v) preparing the independent audit.

195. Applicants further state that the details of the market monitoring proposal will be filed no later than six months before the commencement of WestConnect's operations.

a. Intervenor Comments

196. Several intervenors argue that Applicants' market monitoring proposal fails to meet the requirement of Order 2000 for market monitoring, because the Market Monitoring Unit cannot objectively monitor market participants or WestConnect.¹¹³ They assert that WestConnect should be required to create an independent Market Monitoring Unit that is outside of its authority. Utah Municipals, Western Trading, and the NM Attorney General further state that the market monitoring function is better served by a non-profit entity that will have communication with the Commission when it finds abuses of market power or discriminatory treatment of transmission customers. Certain intervenors assert that

¹¹²The market monitoring provisions and preliminary protocols are included in Appendix H of the WestConnect Tariff.

¹¹³See, e.g., Arizona Consumer Systems, Duke, Dynegy, Enron, NRG, the NM Attorney General, Western Trading, and Utah Municipals.

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WestConnect should adopt the GridFlorida market monitoring model, which was accepted by the Commission.

197. Intervenors also state that Applicants' proposal must be rejected because it only provides a general framework for the activities of the Market Monitoring Unit. They assert that WestConnect, not the Market Monitoring Unit or any other entity, will develop the detailed market monitoring protocols. As a result, WestConnect has the opportunity to minimize the review abilities of the Market Monitoring Unit.

198. The NM Attorney General argues that in order to establish a mechanism that will monitor and mitigate high energy spot prices during peak periods an installed capacity balancing market is needed in Applicants' proposal; if not, there will be no standard to determine when an energy-only price bid will be too high.

b. Applicants' Response

199. Applicants state that the Market Monitoring Unit should report to the Board, which will be independent of all market participants. They also maintain that they are committed to developing market monitoring standards before WestConnect begins operations. Applicants also state that they are working with the California ISO and RTO West to form an independent, centralized, and shared market monitor. They request that the current proposal be reviewed with the understanding that further work needs to be done.

c. Discussion

200. We accept Applicants' proposal for the Market Monitoring Unit as a reasonable interim measure that complies with Order No. 2000 requirements. As discussed in RTO West, Applicants, RTO West, and California ISO, together with transmission customers and public power entities, have formed a Market Monitoring Working Group and are developing a proposal for a West-wide market monitoring entity. The Market Monitoring Working Group has identified several areas of consensus,¹¹⁴ including the following: (1) the Market Monitoring Entity (MME) should be independent from RTOs and market participants; (2) RTO Boards will not act as a screen for MME reports and recommendations; (3) the MME will have a direct relationship with federal, state and provincial regulatory enforcement entities; (4) all RTO markets will be monitored; (5) MME will monitor, identify anomalous market performance, perform studies to determine

¹¹⁴See RTO West at P 202.

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cause, and report results to regulatory and enforcement entities as appropriate; (6) MME will use objective standards and professional judgment to evaluate market performance and identify anomalous market performance; (7) MME will monitor and evaluate RTO market design and, in cooperation with RTO staff, recommend market design and rule changes; and (8) MME will monitor compliance with Commission-imposed mitigation measures and RTO-designed, Commission-approved mitigation measures.

201. The Commission believes that the Applicants' Market Monitoring Unit will be an essential tool in fostering competitive RTO markets. In our Standard Market Design NOPR, the Commission stated that effective market monitoring and market power mitigation are critical elements of the Commission's plan to create and maintain competitive regional bulk power markets.¹¹⁵ The Market Monitoring Unit's effectiveness depends greatly upon its ability to acquire the necessary information provided by market participants. In addition to data obtained from various public sources and in the normal course of operating markets, it may be necessary for the Market Monitoring Unit to request certain other information in order to fully evaluate the competitiveness of markets.¹¹⁶ The Standard Market Design final rule may provide guidance regarding the analytical techniques to be used by the Market Monitoring Unit, including a list of the types of data to be collected. Market monitors must have the ability to request information that will allow them to perform their responsibilities.

202. In New Power Company v. PJM Interconnection, Inc.,¹¹⁷ the Commission required the market monitoring plan to be modified to require immediate disclosure to the Commission when the Market Monitoring Unit identifies a significant market problem that may require: (1) further investigation; (2) a change in the RTO's tariff or market rules; or

¹¹⁵Standard Market Design NOPR, at P 392. We address market power mitigation measures later in this order.

¹¹⁶For example, information on the operating status of transmission and generation facilities where there are claimed outages or de-ratings may be required to analyze allegations of generation withholding.

¹¹⁷98 FERC ¶ 61,208 (2002). This proceeding revealed a gap in the Commission's ability to regulate PJM's and other markets because PJM's market monitoring plan allowed, but did not require, its market monitor to coMarket Monitoring Unitnicate market problems to the Commission on a timely basis.

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(3) action by the Commission and/or one or more state commissions.¹¹⁸ Because Applicants' proposal deviates from the requirements of that order, we direct Applicants to revise their Market Monitoring Plan to include a requirement to report directly to the Commission.¹¹⁹

203. In Order No. 2000, the Commission did not prescribe a particular market monitoring plan or the specific elements of such a plan, because market monitoring is evolving as trading markets are created. The Commission provided for a flexible approach and noted that different market monitoring plans may be appropriate for different RTOs.¹²⁰ In addition, the Commission stated that it would periodically assess the need for, and the degree of market monitoring that should be done.¹²¹ The Standard Market Design NOPR relies heavily on a market monitor that is autonomous from the independent transmission provider to perform a number of specified tasks.¹²² The Commission also indicated that the essential elements of a market monitoring plan would be explored further at technical conference with opportunity for public comments.¹²³ Therefore, we accept Applicants' market monitoring plan with the understanding that the Commission will periodically assess the need for, and degree of, market monitoring for WestConnect.¹²⁴ Accordingly, we encourage Applicants to monitor the outcome of Commission technical conferences regarding the essential elements of a market monitoring plan as they continue to develop such a plan. Furthermore, we urge Applicants to review our recent order in RTO West,

¹¹⁸Id. at 61,759-60.

¹¹⁹Under Applicants' current plan, when market performance is found to be inconsistent with a competitive market, the Market Monitoring Unit will first coordinate its studies with appropriate RTO Staff before it notifies both the Commission and the RTO West Board regarding the inconsistent market performance and the need for further study.

¹²⁰Order No. 2000 at 31,155-56.

¹²¹Id. at 31,380.

¹²²Standard Market Design NOPR, at PP 429-454.

¹²³Id., at P 435.

¹²⁴See Notice Revising Public Comment Schedule and Announcing Technical Conferences, Docket No. RM01-12-000, issued September 10, 2002.

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which discusses the need for developing an independent market monitor¹²⁵ and market power mitigation measures.¹²⁶

204. Finally, we find that the market monitoring plan fails to include the reporting requirements of Order No. 2000 (e.g., how information will be reported and the types and frequency of reports). We direct Applicants to revise their plan to include the modifications discussed above, including specific reporting policies and procedures. Such reporting requirements should be consistent with the requirements identified by our technical conference deliberations.

205. With respect to the NM Attorney General's position, we note that we have neither required the implementation of an installed capacity market in Order No. 2000 nor proposed requiring one in the Standard Market Design NOPR.¹²⁷ Accordingly, we will not require WestConnect to implement such a program for the sake of assisting in the monitoring of its markets and its usefulness in mitigating market power. Furthermore, the Standard Market Design NOPR proposes to replace the use of installed capacity programs through the proposed long-term resource adequacy program described in the proposal. The ability to ensure that adequate capacity is available to serve the marketplace is a fundamental requirement for robust, competitive markets in the long term and a "fundamental pillar of any market design."¹²⁸

M. RTO Function No. 7: Planning and Expansion

The 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; the RTO must

¹²⁵See RTO West, 100 FERC at PP 202-208.

¹²⁶See id. at PP 203 & n.97, 276 (noting that in our Standard Market Design NOPR, the Commission stated that effective market monitoring and market power mitigation are critical elements of the Commission's plan to create and maintain competitive regional bulk power markets.

¹²⁷See, e.g., Standard Market Design NOPR at P 483.

¹²⁸See RTO West at P 275 (quoting California Independent System Operator Corp., 100 FERC ¶ 61,060 at P 120 (2002)).

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coordinate such efforts with the appropriate state authorities. The RTO must have the ultimate responsibility for both planning and expansion within its region.

1. Applicants' Proposal

206. The planning protocol of the WestConnect Tariff describes the framework and process for the expansion and upgrade of the WestConnect grid.¹²⁹ According to Applicants, WestConnect will have final responsibility for the regional transmission expansion plan, subject to approval by relevant regulatory authorities. This plan will be developed by WestConnect with input from the WestConnect transmission planning working group and approved by the Board.¹³⁰

207. Each PTO will be responsible for providing on an annual basis a ten year expansion plan for its service territory. Market participants (including merchant transmission projects) may, at the same time, propose projects for inclusion in the regional transmission expansion plan. WestConnect will consider economic alternatives (such as additions or expansion of generating units) and other options (such as potential replacements for or additions to expansion of planning authority facilities). Under the WestConnect Tariff, PTOs whose systems must be modified or expanded to support a proposed project will have a right of first refusal for the construction and ownership of projects and support facilities that are proposed by either WestConnect or other third parties.¹³¹

a. Intervenor Comments

208. Intervenors argue that a for-profit RTO will be biased towards transmission solutions and will not adequately consider non-transmission alternatives. They contend that the planning protocol does not include non-transmission solutions, such as demand-side management or generation additions, and does not require least-cost solutions. Intervenors also object to PTOs' right of first refusal to construct and own transmission

¹²⁹See WestConnect Tariff, Appendix P (Planning and Expansion Process).

¹³⁰Participation on the WestConnect Planning Working Group is open to all WestConnect stakeholders, WestConnect staff, and other interested parties.

¹³¹See WestConnect Tariff, Appendix P, Sections 7.1(b) and 7.1 (C) (New Transmission Facilities).

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facilities proposed by either WestConnect or third parties. They contend that this allows PTOs to capture the valuable projects and corresponding FTRs for themselves.

b. Applicants' Response

209. Applicants state that the regional transmission expansion plan allows consideration of generating units and other projects as alternatives to expansion of transmission. In addition, section 4 of Appendix P of the WestConnect Tariff (WestConnect Planning Standards and Methodology) provides for a methodology to guide the integrated evaluation of alternatives to transmission. Furthermore, Applicants note that each state in the region will review the relevant transmission projects, making it difficult for an RTO to build inefficient and unnecessary transmission additions.

210. Regarding the provision for the right of first refusal in the regional transmission expansion plan, Applicants state that PTOs retain their responsibility under state law to reliably serve their native load and, therefore, must be able to build and operate the transmission facilities in their service territories. They also maintain that the right of first refusal is required to protect the integrity and reliability of the transmission system and to reduce the liability concerns of PTOs and the RTO. Finally, Applicants reiterate that WestConnect has the ultimate decision-making authority for planning and expansion and that PTOs cannot veto projects that WestConnect decides to build.

c. Discussion

211. With the modifications discussed below, we find that Applicants' proposal meets the planning and expansion requirement of Order No. 2000.

212. RTO expansion plans must be more than a collection of traditional expansion plans developed by individual transmission owners and assembled by an RTO after confirming that they serve reliability needs.¹³² For instance, in PJM, we found that the Commission's long-term competitive goals are better served by RTO expansion plans that allow third party and merchant participation outside the plan. We also determined that third party construction and ownership of new facilities is needed because PJM's proposed structure allows transmission owners, as market participants, to have rights not available to other

¹³²See, e.g., PJM Interconnection, L.L.C., 96 FERC ¶ 61,061 (2001) (PJM); Midwest Independent Transmission System Operator, Inc., 97 FERC ¶ 61,326 (2001).

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parties.¹³³ We believe that Applicants' right of first refusal proposal has not to date been explained or justified, and we direct Applicants to explain why such a proposal is necessary. The presence of multiple potential transmission developers would lower costs to customers. We note that states retain siting jurisdiction and we intend that issues of right of first refusal would not endanger public power private use requirements. We seek further clarification of this feature, including whether it implicates public power private use requirements. Applicants should provide the opportunity for third parties to propose a project at any time that is outside the plan, as long as the third parties assume the risk and WestConnect has the final authority on planning and expansion that may materially affect facilities within the WestConnect footprint.¹³⁴ This will result in transmission expansion that is efficient and cost-effective.

213. We do not agree with intervenors that the proposed planning and expansion protocols preclude the consideration of non-transmission alternatives. Section 4 of Appendix P of the WestConnect Tariff states that the planning standards shall include, at a minimum, consideration of demand forecasts, demand-side projects, and forecasts of resource additions and retirements.¹³⁵ However, we note that Appendix P of the WestConnect Tariff calls for the creation of planning standards to be concluded within one year of WestConnect commencing operations. Accordingly, we condition our finding here on the incorporation of least-cost planning, including demand-side alternatives and generation, in the WestConnect planning and expansion standards.¹³⁶

214. With respect to the arguments that a for-profit entity will favor wires versus non-wire alternatives, we emphasize that an appropriate market monitoring function should include the review of the planning and expansion activities and the Board's decision-making thereon.

¹³³See PJM, 96 FERC at 61,241.

¹³⁴See TRANSLink, 99 FERC at 61,471.

¹³⁵See WestConnect Tariff, Appendix P, Section 3 (WestConnect Planning Objectives).

¹³⁶Any proposal by a third party that remains within the expansion plan that is not identified as a least cost alternative, does not affect the reliability of the WestConnect grid, and does not provide for a duplication of facilities may be undertaken by a third party if that party assumes the risk of constructing the project.

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N. RTO Function No. 8: Interregional Coordination

The RTO must ensure the integration of reliability practices within an interconnection and market interface practices among regions.

1. Applicants' Proposal

215. Applicants state that they will become a member of the Western Electric Coordinating Council and will continue to participate in the Steering Group. They note that the Western Electric Coordinating Council is expected to provide a comprehensive forum for addressing reliability issues.

a. Intervenor Comments

216. Utah Municipals contends that by terminating DesertSTAR, WestConnect has created a new and unnecessary barrier to a seamless market. Utah Municipals further argues that Appendix O of the WestConnect Tariff contemplates a wheeling-out rate that creates seams issues that will hamper the development of a fluid West-wide market, because RTO West will not be charging a wheeling-out rate.

b. Discussion

217. Order No. 2000 requires an RTO to develop mechanisms to coordinate its activities with other regions, regardless of whether or not an RTO exists in those other regions.¹³⁷ If it is not possible to coordinate mechanisms when an RTO proposal is filed, the RTO must propose reporting requirements, including a schedule, and provide follow-up details as to how it will meet the coordination requirements of this function.¹³⁸ In Order No. 2000-A, the Commission stated that we expect parties to use a collaborative process to discuss interregional coordination issues.¹³⁹

218. Consistent with RTO West, we direct Applicants, together with RTO West and the California ISO, to formalize the Steering Group as the resolution group for seams issues

¹³⁷See Order No. 2000 at 31,167.

¹³⁸See id.

¹³⁹See Order No. 2000-A at 31,382.

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among the RTOs in the Western interconnection.¹⁴⁰ We direct Applicants, within 90 days, to: (1) codify the Memorandum of Understanding among the parties to expressly define their commitments and the forum in which issues will be resolved; and (2) provide a list of issues pending before the Steering Group and a time line for resolution of those issues.¹⁴¹

O. Open Architecture

An RTO proposal must not contain any provision that will limit the ability of the RTO to evolve in ways that will improve its efficiency, consistent with the required characteristics and required functions of an RTO.

1. Applicants' Proposal

219. Applicants state that neither the WestConnect LLC Agreement, the WestConnect TCA, nor the Tariff contain any provision that limits the ability of WestConnect to evolve in a manner that will improve its efficiency. Applicants point out that WestConnect has an open door policy for federal, public power, or cooperatively owned transmission systems that wish to participate in WestConnect. Furthermore, the WestConnect LLC Agreement provides that this open door policy will continue until the commencement of WestConnect's operations.

a. Discussion

220. As discussed earlier, we find that the business model developed by Applicants provides flexible terms and conditions to allow virtually any transmission-owning entity to

¹⁴⁰See 100 FERC at P 246.

¹⁴¹This is consistent with our order on calcification in the RTO West proceeding, which is being issued concurrently with this order. See Order Granting Clarification of Prior Order, Avista Corp., et al., 100 FERC ¶ ____ (2002); see also RTO West at P 246.

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participate in WestConnect. Therefore, we conclude that WestConnect meets the requirement of open architecture under Order No. 2000.

P. Cost Benefit

221. Colorado River EDA, a customer of Western, raises concerns over the impact on costs by Western's participation in WestConnect. They state that the Commission should require Applicants to complete a cost-benefit analysis of the proposal.

222. In Order No. 2000, the Commission found that the benefits of RTO formation outweigh the costs, and we did not require individual cost benefit analyses in compliance filings.¹⁴² We will not reverse that determination here. Furthermore, consistent with Snohomish, we will address cost benefit issues when we render a final decision in this proceeding.¹⁴³

Q. Return on Equity

223. In Order No. 2000, the Commission recognized that the risk profile of the transmission business was changing as the industry restructures. The Commission also recognized that the historical data typically used to evaluate return on equity (ROE) may not be reliable since it reflected an industry structure that was different from the one that was being formed. The Commission stated that it believed that, as patterns of transmission ownership and control evolve, new approaches to compensating transmission owners may be appropriate.

224. Consistent with our statements in Order No. 2000 and in order to encourage progress in getting WestConnect in operation in a timely manner, we are open to the idea of allowing the transmission owners in Westconnect's footprint the opportunity to earn an incentive ROE when WestConnect becomes operational. In this connection, we note that, recently, in Midwest Independent System Operator, Inc., 100 FERC ¶ 61,292 (2002), we allowed the Midwest ISO's participating transmission owners to receive an upward

¹⁴²See Order No. 2000 at 31,017, 31,036.

¹⁴³See Public Utility District. No. 1 of Snohomish County, Washington v. FERC, 272 F.3d 607, 619 (D.C. Cir. 2001) (Snohomish); see also RTO West, 100 FERC at P 263.

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adjustment of 50 basis points in their ROEs for turning over the operational control of their transmission facilities.¹⁴⁴

The Commission orders:

(A) Applicants' petition for declaratory order is hereby granted in part, as discussed in the body of this order. The Commission makes no findings with regard to any other issue or proposal raised by this filing.

(B) The motion to intervene out of time in this proceeding is hereby granted, as discussed in the body of this order.

(C) Applicants' answer to the comments and protests in this proceedings and its supplements to its answer are hereby granted, as discussed in the body of this order.

(D) Applicants are hereby directed to, within 90 days of the date of this order: (1) codify the Memorandum of Understanding and Cooperation between the parties to expressly define their commitments and the forum by which issues will be resolved, and (2) provide the Commission a list of pending issues before the Steering Group and a time line for resolution of those issues, as discussed in the body of this order.

By the Commission. Chairman Wood, Commissioner Breathitt and Commissioner Brownell concurring in part with a separate statement attached.
(S E A L) Commissioner Massey dissenting in part with a separate statement attached.
Commissioner Breathitt dissenting in part with a separate attached.

Magalie R. Salas,
Secretary.

¹⁴⁴The Commission has indicated that it intends to address this matter in a separate policy statement.

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Appendix A

Timely and Untimely Motions and Notices to Intervene.

Motions to intervene out of time are indicated by asterisk after the name of the party.

American Wind Energy Association
Arizona Power Authority
Avista Corporation
Bonneville Power Administration
British Columbia Hydro and Power Authority
California Independent System Operator, Inc.
Colorado Association of Municipal Utilities
Colorado River Energy Distributors Association
Colorado Springs Utilities
Deseret Generation and Transmission Cooperative, Inc.
Dynergy, Inc.
El Paso Merchant Energy, LP
IDACORP Energy L.P.*
Imperial Irrigation District
Industrial Customers of Northwest Utilities
Metropolitan Water District of So. California
Modesto Irrigation District
M-S-R Public Power Agency
National Rural Electric Cooperative Association
Nevada Power Company and Sierra Pacific Power Co.
New Mexico Industrial Energy Consumers
New Mexico Public Regulation Commission
PacifiCorp/Puget Sound and Idaho Power
PG&E National Energy Group
Pinnacle West Capital Corp, Pinnacle West Energy Corp., and APS Energy Services
Power Up Corporation
Public Power Council
PUD No. 1 of Snohomish County, Washington
Southern California Edison Company
Transmission Agency of Northern California
Valley Electric Association
XCEL Energy Services, Inc.

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Appendix B

Motions to Intervene, Protest, and/or Comment

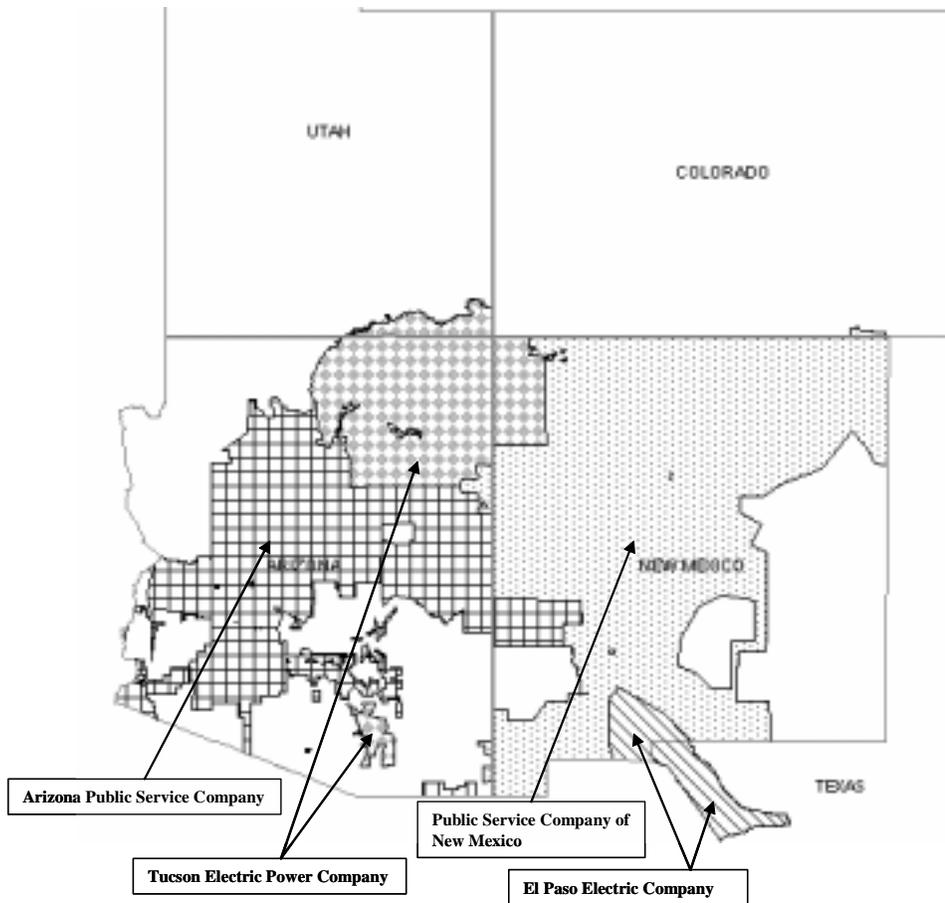
Arizona Consumer-Owned Electric Systems (Arizona Consumer Systems)
Attorney General of New Mexico (NM Attorney General)
Basin Electric Cooperative (Basin)
Calpine Corporation (Calpine)
Colorado River Energy Distributors Association (Colorado River EDA)
Constellation Power Source, Inc. (Constellation)
Department of the Air Force - United States Executive Agencies (US Executive Agency)
Duke Energy North America, LLC and TECO Power Services Corporation (Duke)
Electric Power Supply Association (EPSA)
Enron Power Marketing, Inc. (Enron)
Mirant Americas Energy Marketing, LP, Mirant California, LLC, Mirant Delta, LLC,
and Mirant Potrero, LLC. (Mirant)
Navajo Tribal Utility Authority (Navajo)
Nevada Independent Energy Coalition (Nevada Coalition)
Northwest Requirements Utilities (NW Utilities)
NRG Power Marketing, Inc. (NRG)
PNGC Group (PNGC)
Public Power Council (Public Power)
225. Reliant Energy Power Generation, Inc. (Reliant)
Salt River Project Agricultural Improvement and Power District (Salt River)
Southwest Transmission Cooperative, Inc. (Southwest Transmission)
Tractebel Energy Marketing, Inc. and Tractebel Power, Inc. (Tractebel)
Tri-State Generation and Transmission Association, Inc. (Tri-State)
Utah Associated Municipal Power Systems (Utah Municipals)
Western Area Power Administration (Western)
Western Power Trading Forum (Western Trading)

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Appendix C

Map of WestConnect Region, As Proposed



Source: RDI PowerMap

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Arizona Public Service Company
El Paso Electric Company
Public Service Company of New Mexico
Tucson Electric Power Company

Docket No. RT02-1-000

WestConnect RTO, LLC

Docket No. EL02-9-000

(Issued October 10, 2002)

WOOD, Chairman, BROWNELL, Commissioner, BREATHITT, Commissioner
concurring in part

We are pleased that today's order finds acceptable the WestConnect RTO Applicants' proposed scope and configuration. We believe that this decision, in conjunction with other guidance provided in the order, provides a solid framework from which the Applicants together with non-public utility entities and other market participants in the Southwest can begin to develop an efficient, competitive and seamless electric market. Our decision today is bolstered by the time and effort committed to the WestConnect proposal by non-public utilities such as Western Area Power Administration and the Salt River Project Agricultural Improvement and Power District. We encourage the WestConnect Applicants to continue their dialogue with all transmission owners in the region to further expand the scope of the WestConnect RTO.

We respectfully concur.

Pat Wood, III
Chairman

Nora Mead Brownell
Commissioner

Linda K. Breathitt

Commissioner

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Arizona Public Service Company
El Paso Electric Company
Public Service Company of New Mexico
Tucson Electric Power Company

Docket No. RT02-1-000

WestConnect RTO, LLC

Docket No. EL02-9-000

(Issued October 10, 2002)

MASSEY, Commissioner, dissenting in part:

I applaud the progress that market participants are making toward grid regionalization in the Southwest and encourage them to continue. Today's order makes some important decisions and provides appropriate guidance regarding those efforts. I support most aspects of today's order. WestConnect, with its current membership, is a vast improvement over the status quo, and nothing I write today should be construed otherwise.

There are two aspects of this order that I do not support. I do not agree with the order's acceptance of the scope and configuration of WestConnect as it stands today. Our regulations require that an RTO be of sufficient scope and configuration to effectively perform its required functions.¹⁴⁵ Indeed, Order No. 2000, the touchstone of today's order, states that the ability of an RTO to perform its functions effectively is the principal consideration in evaluating an RTO's scope,¹⁴⁶ and that to satisfy the scope and

¹⁴⁵18 CFR § 35.34(j)(2). (2002)

¹⁴⁶Regional Transmission Organizations, FERC Stats. & Regs. ¶ 31,089 (1999) at 31,082.

configuration characteristic "all or most of the transmission facilities in a region must be included in the RTO."¹⁴⁷

WestConnect, with its current membership, does not meet these standards. I am informed by Commission staff that some of the non-participants, especially Western and Salt River, control significant grid assets that are intermingled with those of the participants. In fact, these two transmission owners are major transmission players in the region. Their absence carves gaping holes in WestConnect's scope and configuration. Without control over these assets, WestConnect's configuration will not permit it to perform effectively such critical RTO functions as congestion management, parallel path flow management, and planning and expansion. I also fail to see how such a configuration would provide customers with one-stop shopping for transmission service in the Southwest. Order No. 2000 underscores the importance of these RTO characteristics and functions. Therefore, I would withhold acceptance of WestConnect's scope and configuration at this time and commit Commission mediation resources to bringing the missing transmission owners on board.

I also do not agree with the Commission's adoption of a significant policy shift that, in the limited time I have had to consider it, strikes me as ill advised. Paragraph four of the order states that "unless the Commission has specifically indicated in this order that an element of the RTO proposal is inconsistent with the Standard Market Design proposal or needs further work in light of the Standard Market Design proposal, we do not intend, in the final Standard Market Design rule, to revisit prior approvals or acceptances of RTO provisions because of possible inconsistencies with the details of the final rule." In other words, unless we have explicitly flagged an aspect of the WestConnect proposal in this order, it is immune to whatever we adopt in the SMD final rule.

This declaration unnecessarily ties the Commission's hands in developing regional electricity markets. My strong support for our SMD rulemaking was based on an expectation that the best elements of market design would be identified and would become the standard for wholesale markets. Of course, regional variations on the standard would be allowed where needed to accomplish the objectives of our SMD initiative. Also, we have said that our debates and decisions with respect to evolving RTO policy would inform our SMD policy (and vice versa). But with today's order, before we have finalized a standard, indeed before we have even received any formal comments on the SMD NOPR, the Commission is determining key regional standards in RTO orders and binding itself not to change its mind, even if the forthcoming NOPR

¹⁴⁷See *id.* at 31,086.

comments (including an extensive outreach process) lead us to conclude that other standard terms or other regional variations would be more appropriate. Moreover, it is no secret that, because RTO formation is voluntary under Order No. 2000, the Commission has taken a liberal approach to accepting less than state of the art RTO proposals with the objective of encouraging regions to progress toward RTO formation. I am concerned that subordinating aspects of our SMD policy to provisions agreed to in RTO venues risks compromising the objectives of SMD: eliminating undue discrimination, ensuring customer protection, and creating seamless efficient wholesale electricity markets.

Promising not to revisit certain decisions is a highly unusual administrative procedure that gives me great concern. Many unforeseen factors could render today's decisions ill advised. As a regulator and policy maker, I must remain open to reconsidering decisions in light of new information and our evolving policy. Policy evolution has been constant during my two terms as a Commissioner. An evolving policy, within applicable legal authority, allows a regulatory agency to keep pace with the changing times.

For these reasons, I dissent in part from this order.

William L. Massey
Commissioner

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Arizona Public Service Company
El Paso Electric Company
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Tucson Electric Power Company

Docket No. RT02-1-000

WestConnect RTO, LLC

Docket No. EL02-9-000

(Issued October 10, 2002)

Breathitt, Commissioner, dissenting in part:

Although I believe that this order should give some assurances that we are listening to Western entities and deferring to their hard sought compromises, there is one issue on which I will be dissenting. For the most part this order accepts, at least for Day 1 implementation, the plan set forth in the WestConnect filing. This plan that has been about five years in the making is not completely finalized, but represents a lot of hard work on the part of interested parties that seek to have an RTO in the desert southwest. I hope all of these parties, including the public power entities, see today's order as a milestone along the way to completing this process and not a roadblock to their participation.

I am issuing a partial dissent on the issue of governance. Today's order requires five changes to the provisions governing the relationship between the Board and the Stakeholder Advisory Committee. I felt that the governance section of the SMD NOPR was too prescriptive. I am not sure that we needed a section on governance in that NOPR when we have provisions in Order 2000 on independence that I believe adequately cover governance issues.

I believe that this order goes well beyond the requirements of Order 2000 in four of the required changes to the governance proposal. In this instance, I support a change to require majority voting in selecting board candidates rather than using a peremptory strike method, and I feel that this change alone ensures independence. The order also requires the addition of two stakeholder groups and requires two voting representatives from each stakeholder group on the Board Selection Committee. These required changes are unnecessarily prescriptive. Today's order also directs Applicants to remove language related to ensuring appropriate qualifications for stakeholder group membership and requiring a quorum for issues to be taken before the Board. These directives may seem minor, but I believe that the more prescriptive we are the more likely we are to upset the careful balance that has been struck between those entities that are before us seeking to form the WestConnect RTO. For these reasons I respectfully dissent on the governance section.

Linda K. Breathitt
Commissioner