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Energy

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FERC Acts on Natural Gas Transparency Reporting, Electricity Transmission Pricing, and Capacity Markets

At its September 18, 2008 meeting, FERC clarified certain aspects of its natural gas transparency reporting rule, approved incentive rates for a privately financed transmission line in New York, accepted a proposal for an experimental region-wide rate for non-firm transmission in the Southwestern U.S., and dismissed a complaint regarding capacity auction prices in the PJM market.

Gas transparency reporting requirements clarified and one-time "safe harbor" established

In Order No. 704 issued last year, FERC adopted rules that required natural gas wholesale market participants, including some entities not otherwise subject to FERC's jurisdiction, to report annually summary information about their physical transactions, both sales and purchases (Docket No. RM07-10). Data is to be reported in new Form No. 552. The rule had its genesis in the Energy Policy Act of 2005, which authorized FERC to "facilitate price transparency in markets for the sale or transportation of physical natural gas in interstate commerce."

Order No. 704-A reiterates that the focus of the data collection is transactions that utilize an index price, contribute to index price formation, or could contribute to index price formation. The Commission clarified that this includes volumes that use next-day or next-month price indices, volumes that are reported to a price index publisher, and volumes that could be reported to an index publisher, even if the respondent does not report to a publisher. The latter is meant to include bilateral, arms-length, fixed price physical transactions between non-affiliated companies at all trading locations, even those transactions that do not occur at locations designated by an index publisher.

FERC established a one-time "safe harbor" for the 2008 Form No. 552. It determined that respondents submitting the form in 2009 will benefit from a rebuttable presumption that the data provided is accurate and submitted in good faith. Further, FERC held that it does not intend to penalize respondents for errors in reporting on Form No. 552, provided that respondents use reasonable efforts to comply with the regulations and instructions for Form No. 552.

The Commission made the following additional significant modifications and clarifications to the original rule:

- Sales and purchases cannot be netted against each other in order to qualify for the *de minimis* exemption threshold of 2.2 million MMBTu of transactions. The *de minimis* exemption does not apply to entities that hold blanket certificates.

- Form No. 552 will collect data only on those end-use transactions that rely on price indices or that could be used to form a price index. Traditional bundled sales by an LDC at a state-approved rate are not subject to reporting.

- Transaction data need not be segregated by specific price index location.

- Balancing, cash-out, operational and other similar transactions must be reported if they rely upon, contribute to, or could contribute to a price index.

Incentive rates for major new transmission line approved

FERC granted a 275 basis point return-on-equity adder to the rates for a new 190-mile high voltage transmission line that is expected to increase by 1200 NW the transfer capability between upstate New York and the Hudson Valley and points south. The project will be developed and owned by New York Regional Interconnect, Inc., (NYRI), a privately owned corporation. The incentive rate is intended to enable NYRI to attract the investment needed to develop the $2 billion project, and will be added to an ROE to be determined later by the FERC.

The incentive is comprised of 50 basis points for future membership in the New York ISO, 100 basis points for forming an independent transmission company (transco), and 125 basis points for the risks faced in completing the project and for using advanced technologies (HVDC transmission line, fiber-optic cables, undergrounding a portion of the line, and a static VAR compensator). The incentives are conditioned on the New York Public Service Commission finding that the project either ensures reliability or reduces congestion, and approving siting for the project. Incentive rates for transmission lines have been a divisive issue among the Commissioners but this order received unanimous support.

Regional rates for experimental non-firm transmission service approved

The Commission approved a two-year experimental transmission service to be offered by an association of transmission owners in the Southwest, known as WestConnect (Docket No. EL08-68). Customers would be offered the option of buying a new non-firm hourly coordinated transmission service across the WestConnect participants' systems at a single transmission rate instead of buying standard OATT non-firm service at individual pancaked rates. Customers would pay the highest OASIS-posted ceiling rate of any of the WestConnect participants involved in the transaction. Participants providing service would be allocated a *pro rata* share of revenues, and no provider will collect more than its posted ceiling rate. Participants may withdraw from the experiment upon certain conditions.

This service is a step toward regional coordination by utilities that have declined to take the organized market approach to regional coordination. Indeed, their petition in this case says they do not contemplate creating an RTO or ISO. The experiment is to see how the alternative service might affect the use of available transfer capability and the revenues of the participants.

PJM capacity market complaint dismissed

The Commission dismissed a complaint by various state commissions, consumer advocates, and wholesale buyers that alleged capacity prices determined in recent PJM auctions were excessive and should be altered (Docket No. EL08-67.) PJM's Reliability Pricing Model (RPM) was established two years ago to hold annual auctions to secure sufficient resources for a reliable supply of electricity during a delivery year three years after the auction. The complaint was directed at three "transitional" auctions that had lead times less than three years before the delivery year. The complaint asserted that there was no price discipline provided by new capacity resources due to the short lead time before the delivery year, that certain auction parameters were deficient, and that suppliers had the discretion to withhold supply to drive up prices.

In dismissing the complaint, FERC found that no party violated the PJM tariff and that the auction prices were determined in accordance with the tariff rules, including the market power bid mitigation procedures.

In the order, FERC put its thumb firmly on the scale for price certainty: "Changing a rate and quantity already determined in accordance with existing tariff provisions on which parties have relied would defeat the purpose of the forward binding commitment, and undo the incentives for new capacity resources....The prices and obligations set in those auctions became set as of the date of the auctions, and PJM and the capacity resource providers had every right to rely on those prices and obligations in making their decisions, including any capacity commitments and investment decisions."

The Commission did, however, issue a separate order that puts some teeth into a PJM stakeholder process to consider RPM auction reforms (Docket No. ER05-1410.) In June 2008, a PJM consultant (the Brattle Group) issued an evaluation of RPM that touched on many of the issues raised by the complainants and suggested areas for reform. A PJM stakeholder process is already considering possible reforms. FERC identified a number of specific reforms from the Brattle Report that it expects PJM and the stakeholders to address, and ordered PJM to file a report by December 15, 2008 explaining why reform on the identified issues could not be made in time for the next auction in May 2009. A technical conference will be held in February 2009.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our energy practice group:

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