

**UNITED STATES OF AMERICA 90 FERC ¶ 63,004
FEDERAL ENERGY REGULATORY COMMISSION**

**Central Hudson Gas & Electric Corporation
Consolidated Edison Company of New York, Inc.
Long Island Lighting Company
New York State Electric and Gas Corporation
Niagara Mohawk Power Corporation
Orange and Rockland Utilities, Inc.
Rochester Gas and Electric Corporation and
New York Power Pool**

**Docket Nos. ER97-1523-011
OA97-470-010
ER97-4234-008**

**CERTIFICATION OF QUESTION REGARDING RETENTION OF
QUALIFYING FACILITY STATUS BY A FACILITY
THAT COMPLIES WITH ISO TARIFF**

(Issued February 8, 2000)

TO THE COMMISSION:

Pursuant to Rule 714 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 714 (1999), I hereby certify to the Commission for determination the following question:

Will a facility that otherwise qualifies under Section 3(18) of the Federal Power Act, the Commission's implementing regulations, and relevant decisional precedent as a "Qualifying Facility" ("QF") be disqualified as a QF (and hence the power produced by the facility may not qualify as QF power) as a result of the QF's compliance with the energy balancing provisions of the New York Independent System Operator, Inc.'s Open Access Transmission Tariff ("NYISO OATT"), the NYISO Market Administration and Control Area Services Tariff ("NYISO Services Tariff") and the NYISO's rules and practices (collectively, "NYISO Rules") such that the QF is deemed to purchase [and resell] imbalance power from the NYISO whenever its output is less than the amount it has scheduled for sale to certain customers and/or into the NYISO Locational Based Marginal Price market?

For the reasons set forth below, the recommended answer is no.

BACKGROUND

This question arises in the context of the filing by the Member Systems of the New York Power Pool¹ of unilateral amendments to existing transmission agreements of a number of participants in the New York markets now administered by the NYISO, which have been set for hearing by the Commission's September 30, 1999 order in these proceedings. The case has been proceeding under a three track schedule with the first track, through January 31, 2000, being a settlement judge process. In that settlement process, at least one QF that has an existing contract with a Member System of the New York Power Pool expressed concern about the implications for its QF status of an agreement to comply with the NYISO's tariffs, and particularly its energy balancing rules and practices. While working toward a stipulation of settlement that would resolve issues between it and the Member Systems, it has been made clear that any such stipulation would be contingent upon receipt by the QF of a satisfactory answer to the question posed above.

On January 4, 2000, I received a request filed by Selkirk Cogen Partners, L.P. ("Selkirk") that I certify the question posed above to the Commission for a determination under the provisions of Rule 714. Selkirk also supplied a supporting memorandum. On January 6, 2000, a similar request was received from Lockport Energy Associates, L.P. ("Lockport"). A prehearing conference was convened on January 6, 2000, for the purpose, among other things, of receiving oral views of the parties on the requests of Selkirk and Lockport. At that conference, views of other parties were received and I asked for a supplemental memorandum that explored in more detail possible arguments that could be advanced against the result sought by Selkirk and Lockport. That memorandum was filed on January 20, 2000.

The following sets forth the relevant issues, the views of the parties and my recommendation for disposition. It is respectfully requested that the Commission expedite consideration of this question because settlement of issues involving several parties in this proceeding are dependent upon receipt of a satisfactory answer.

RELEVANT ISSUES

¹ Now described as Members of the Transmission Owners Committee of the Energy Association of New York State. In this document, I will continue to refer to this party as Member Systems of the New York Power Pool.

As set forth by Selkirk, the Selkirk cogeneration facility ("Selkirk Facility") in the Town of Bethlehem, New York, has a Demonstrated Maximum Net Capability ratings of 360 MW (summer) and 414 MW (winter). It has been certified as a QF. It sells 79.9 MW of its output to Niagara Mohawk Power Corporation ("Niagara Mohawk") and 265 MW to Consolidated Edison Company of New York, Inc. ("Con Edison") under long term contracts. Currently, Selkirk states that there are 40-100 MW not committed under these long term contracts that is available to be sold by Selkirk into the NYISO-administered market.

Under its OATT, the NYISO offers Energy Imbalance Service, which a transmission customer serving load within the NYISO's control area, or for an export transaction when the generation source is located in the NYISO control area, must purchase from the NYISO. Under the NYISO Service Tariff, real time deviations from scheduled energy in either bi-lateral transactions or in the Locational Based Marginal Pricing ("LBMP") market are subject to real time market settlement based upon LBMP prices. Selkirk is concerned that NYISO-furnished imbalance service supplied under the terms of the NYISO's Tariffs might lead to disqualification of the Selkirk Facility in that the NYISO will, under an automatically triggered provision, make up the difference to the load-serving entity if a generator's production is less than the amount scheduled for sale. Thus, Selkirk would be deemed to have purchased the differential from the NYISO and then to have resold it to its purchasers.

There is in the NYISO's tariff a so-called "PURPA Exception," under which, for certain contracts, the QF will be treated as being in balance under the NYISO's rules for all bilateral transactions where the purchasers are obligated to purchase market energy only if they require it to meet their real-time load. As a consequence, the NYISO does not provide power to the excepted QF's purchaser in excess of the amount actually produced, and the QF is not deemed to have purchased and resold such excess power to the third-party purchaser. Selkirk's contracts with Niagara Mohawk and Con Edison are subject to the PURPA Exception.

The PURPA Exception does not apply outside of the bilateral contract regime, for example, to so-called "merchant" power transactions where the QF is scheduling power into the NYISO LBMP market, or where the QF's purchaser under a bilateral contract does not agree to the retroactive reduction in the scheduled amount. For scheduled merchant power transactions where the delivered amount is less than scheduled, the NYISO would automatically make up the difference and deems this increment to have been sold by the QF, and this transaction would not qualify for the PURPA Exception.

IEWS OF THE PARTICIPANTS

SELKIRK

Selkirk points out that it owns a facility that meets all of the requirements to be a QF and is currently certified as a QF. The only change is that now, in order to participate in the NYISO market, it must comply with the NYISO Rules relating to its merchant power transactions. Short of withdrawing as a supplier in the NYISO LBMP market, Selkirk cannot avoid the NYISO Rules. These rules, part of a jurisdictional tariff, should not be read to require Selkirk to relinquish its QF status in order to compete on a par with other suppliers in the NYISO market, it contends.

Selkirk sees its situation here as analogous to the situation in which QFs were held to have been wrongfully excluded from eligibility for firm wheeling services in the PacifiCorp/Utah Power & Light Company merger. Environmental Action, Inc. v. FERC, 939 F.2d 1057, 1062 (D.C. Cir. 1991) (quoting Utah Power & Light Co. et al., 47 FERC ¶ 61,209 at 61,740 (1989)). Selkirk further maintains that, in Order 888-A, the Commission clarified that a QF arrangement for receipt of Real Power Loss Service or ancillary services from the transmission provider or a third party for the purpose of completing a transmission transaction is not a sale-for-resale of power by a QF transmission customer that would violate its QF rules.² This order recognized the unique regulatory status of QFs in transmission transactions in the new competitive marketplace, and the importance of not jeopardizing the ability of QFs to compete with other suppliers, Selkirk argues.

Selkirk also cites in support of its position here Connecticut Valley Electric Co., Inc. v. Wheelabrator Claremont Co., L.P., et al., 82 FERC ¶ 61,116 (1998), order denying reh'g and reconsideration and granting in part and denying in part clarification, 83 FERC ¶ 61,136 (1998), appeal docketed, Connecticut Valley Electric Co. v. FERC,

²Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888-A, 62 Fed. Reg. 12,274 at 12,310 (March 14, 1997) III FERC Stats. & Regs. ¶ 31,048 (1997), order on reh'g, Order No. 888-B, ¶ 61,248 (1997), order on reh'g, Order No. 888-C, 82 FERC ¶ 61,046 (1998), appeal docketed, Transmission Policy Group v. FERC, et al., Nos. 97-1715, et al. (D.C. Cir. Dec. 5, 1997)

No. 98-1294 (D.C. Cir. June 30, 1998). In that case, the Commission considered the purchase of make-up power from Pennsylvania Electric Company ("Penelec") by Penntech Papers, Inc. ("Penntech"), a QF with a power purchase agreement with Niagara Mohawk Power Corporation, to be an energy imbalance ancillary service that would not affect Penntech's QF status. Selkirk maintains that the provision of make-up or balancing service by the NYISO is separate and distinct from transmission service and does not constitute a sale for resale. The fact that it must make a cash payment to the ISO should not affect the result, Selkirk contends, noting that QFs are permitted to purchase line loss service without jeopardizing QF status.

Finally, Selkirk states that it is not attempting under this arrangement to sell more than its actual net output. Answering the question posed in the negative will not give it an advantage over other suppliers because the price for Selkirk's merchant power will be dictated by the market.

LOCKPORT

Lockport also seeks certification of the identical question, urging an identical negative answer. In its filing, Lockport states that it owns a 200 MW QF in Lockport, New York, and has a power purchase agreement with New York State Electric & Gas Corporation ("NYSEG"). It has the right under that contract to dispatch a portion of its output during certain times of the year as merchant power into the New York wholesale competitive electric market.

Lockport points out that if it wishes to sell merchant power into the NYISO-administered markets, it must take service under the NYISO OATT and/or the NYISO Services Tariff. Both provide procedures for balancing scheduled energy deliveries with actual deliveries. The NYISO Services Tariff provides for a two settlement system – a day-ahead market and a real time market. A generator is financially obligated to provide 100 percent of the power it committed to deliver in the day-ahead market to the NYISO spot market or through a bi-lateral arrangement with a third party purchaser. If it delivers less power in the real time market than it scheduled in the day-ahead market, it must pay for the imbalance by purchasing the energy from the NYISO at the real time LBMP price. Generators taking service under the OATT must pay a charge equal to the greater of 150 percent of the real time LBMP or \$100/Mwh for withdrawals under scheduled withdrawals.

Lockport notes that its sales of energy to NYSEG under its power purchase agreement are not subject to the energy imbalance provisions of these NYISO tariffs because the PURPA Exception described above provides a retroactive adjustment for a

QF's PURPA deliveries. That exception does not apply to the non-PURPA deliveries of merchant power into the competitive wholesale market.

Lockport also finds support in Connecticut Valley for its view that its purchase of energy imbalance service in these circumstances is not a sale for resale of power produced by a facility other than a QF. Lockport also cites to the provisions of Order 888-A, discussed above, which it contends are in accord.

Lockport concludes that the purchase of make-up power from the NYISO to balance scheduled deliveries with actual production is the purchase of an ancillary service which also supports the efficient transmission of energy in the wholesale competitive market. Since it is not selling more than its actual output when it purchases power from the ISO to make up for inadvertent delivery shortfalls, Lockport maintains that this arrangement should be treated by the Commission as Penntech's was in Connecticut Valley.

OTHER PARTIES

At a prehearing conference held on January 6, 2000, other participants in these proceedings were offered the opportunity to express their views orally on the issue presented for certification. Sithe/Independence Energy Partners, L.P. ("Sithe") stated that, in its view, the type of imbalance service involved here is permissible under applicable precedent. It supports the rationale and answer suggested by Selkirk and Lockport. Moreover, it would like to have this result applied to Sithe's Independence plant for all of the same reasons advanced by Selkirk and Lockport.

Indeck-Corinth L.P. ("Indeck") conveyed its understanding that the question was intended to be of generic applicability, so that it would apply to similarly situated QFs, like Indeck, and not only to those plants specifically mentioned in the filed requests.

After some initial uncertainty, which was later clarified, the Member Systems advised that they support the request for certification and recommended answer in the context of reaching a settlement with the QFs involved here, and, in the event that no settlement is reached, that they would remain silent on the matter.

Because it appeared that arguments could be advanced in opposition to the recommended answer, and none were forthcoming at the conference, I asked for a brief submission outlining the other side of the issue in order to present the Commission with a balanced and objective analysis of the question. The Discussion and Conclusion below reflect consideration of the memorandum filed in support of a negative answer to the

question by Selkirk and Lockport, the stenographic transcript pages 92-105 of the prehearing conference held on January 6, 2000, and the "devil's advocate" submission of possible opposing arguments ordered by the undersigned at that conference.

DISCUSSION AND CONCLUSION

Selkirk and Lockport raise the following arguments to support their position that the question should be answered in the negative.

Connecticut Valley

The supporting memoranda rely on the Commission's finding in Connecticut Valley that a QF would not lose its QF status if it purchased service from the transmission provider to correct for imbalances between scheduled energy and load. There, the Commission found that a QF's purchase of power from its transmission provider to make up for inadvertent delivery shortfalls was the purchase of an ancillary service as defined in Order No. 888 and 888-A, and, as such, did not result in the QF's engaging in a sale-for-resale of power produced by a facility other than a QF. The Commission explained:

In Order No. 888, the Commission determined that the "energy imbalance service" is one of six ancillary services which must be provided under an open access transmission tariff. The description of "energy imbalance service" and the service provided by Penelec [the transmission utility] to Penntech Papers [the QF] to correct inadvertent imbalances indicate that they are the same service. As this is an ancillary service as defined in Order No. 888 and 888-A, it does not constitute a sale-for-resale and does not affect Penntech Papers' QF status. 82 FERC at ¶ 61,422-23.

Both Selkirk and Lockport see a ready parallel between the instant situation and the one that was before the Commission in Connecticut Valley. Factors supporting the parallel view are: (1) the service provided by the ISO here is a type of energy imbalance service like that provided by Penelec to Penntech Papers in Connecticut Valley; (2) the ISO here is acting like the transmission provider [Penelec] in Connecticut Valley by requiring the purchase of a make-up service that is separate and distinct from transmission service; (3) like Penntech Papers, the QFs here are not attempting to sell more than their actual net output when they purchase power from the ISO to make up for inadvertent delivery shortfalls – they will schedule no more than their Demonstrated Maximum Net Capability ("DMNC"); and (4) the energy balancing service that Penntech Papers purchased from Penelec was designed to correct a mismatch between energy scheduled by the QF and energy generated by the QF, just as here, the imbalance service

required by the ISO is to correct a mismatch between energy scheduled into the day ahead market by the QFs and the actual real-time deliveries by the QFs.

There are, however, two factors that distinguish this case from Connecticut Valley: (1) in Connecticut Valley, the ancillary service was provided by a transmission utility to balance power output with the amount scheduled under a long term contract between the QF and the purchasing utility, whereas here the service is provided by an ISO for the purpose of supporting non-bilateral sales of energy into the wholesale competitive market; and (2) in Connecticut Valley, Penntech's obligation to purchase energy imbalance service arose under a transmission utility's tariff, although not an open access transmission tariff, whereas here, it arises under the NYISO's Services Tariff.

It must be determined whether, in light of these distinctions, the result reached by the Commission in Connecticut Valley can apply to the facts here. Perhaps the most significant distinction arises from the context of the transaction, *i.e.*, that the imbalance service provided to Penntech by Penelec was offered by the transmission provider to facilitate a PURPA power sale, and, therefore, was more clearly the type of ancillary service envisioned by the Commission in its Order 888-A than the service provided here by the NYISO. Here, it takes a little greater effort to see that the transaction is essentially similar and ought to be treated similarly. This is partly because the PURPA piece of the puzzle is not in issue, due to the "PURPA exception" noted above. It is the secondary transaction, where the QF is seeking to engage in non-bilateral sales in the competitive bulk power market, that muddles the picture. But, stripped down to its essentials, the transaction seems very similar to Penntech's in Connecticut Valley.

The Commission found in Connecticut Valley that the incidental purchase of make-up power for correction of inadvertent imbalances, necessary in the context of a QF using transmission service for delivery of its power to another entity, was an ancillary service as defined in Order Nos. 888 and 888-A, and did not affect the QF's certification. The basic decisional underpinnings of the Penntech issue in Connecticut Valley are apparent here. The NYISO's energy imbalance service is a requisite offering for generators wishing to participate in its markets, as Penntech's transmission arrangements with Penelec were required to complete the PURPA sales transaction. So, like in the Penntech situation, the QFs here may be placed in the position of making incidental purchases of make-up power in order to complete a transaction. While not in the context of a transmission arrangement to facilitate a PURPA sale as in Penntech, the purchase of make-up power by the QFs here is virtually an identical situation to the one in Connecticut Valley for all relevant purposes.

That the service here is offered by the NYISO and not under a transmission provider's OATT likewise does not seem of any real consequence. The Commission's efforts to nurture effective competitive wholesale electric markets has resulted in the establishment of new institutions, such as ISOs and RTOs to help ensure that transmission is provided to market participants openly and free of undue discrimination. These institutions, in turn, have developed Open Access Transmission Tariffs, and in the case of the NYISO, a Services Tariff that lays out responsibilities of market participants. The NYISO has assumed market facilitation responsibilities performed more narrowly in the past by transmission utilities. The NYISO's energy imbalance service requirement is similar to the ancillary imbalance service offered under the previous industry structure by the transmission provider in that it supports the efficient transmission of energy. Instead of the more narrow role of imbalance service provided by a transmission utility to support bilateral contract sales, the NYISO imbalance service here supports the efficient transmission of energy into the wholesale competitive market. Accordingly, the NYISO's involvement does not provide a basis for treating the QFs here differently than in Connecticut Valley.

Finally as to the Connecticut Valley analysis, a key issue is whether the purchase of power by a QF from the NYISO LBMP market to make up for shortfalls in committed deliveries to the NYISO, for power bound for merchant transactions other than PURPA contract fulfillment, constitutes a sale for resale of power produced by a facility other than a QF and, hence, prohibited by QF certification rules. In the Penntech issue in Connecticut Valley, the Commission saw that the make-up energy purchase was only incidental and intended to cover unanticipated imbalances, in the context of a net output sale. So, even though it was clear that some incidental amount of output purchased from the transmission entity and later sold by the QF would not have been solely produced by the QF, the Commission found that the transaction would not affect Penntech's QF status. There is nothing in the instant situation that requires a different conclusion. The purchase of an energy imbalance service from a transmission company or an ISO in the current circumstances should not affect QF status.

Access to the markets

Selkirk has argued that it cannot avoid the NYISO's rules that require the purchase of energy imbalance service and participate in the NYISO's LBMP market. It contends that the tariff should not be read in a manner that forces it to relinquish its QF status in order to compete on an equal footing with other suppliers in that market. Selkirk draws an analogy to Environmental Action, where the Court criticized a Commission decision to deny QFs access to firm wheeling services in the

PacificCorp/Utah Power & Light Company merger so as to place QFs on an essentially equal footing competing suppliers, suggesting that denial of access to QFs would effect an administrative repeal of the congressional choice to encourage the sale of power by QFs.

Similarly, Selkirk contends that Order No. 888-A recognizes the unique regulatory status of QFs with respect to transmission issues arising in the new competitive marketplace in language clarifying that "a QF arrangement for receipt of Real Power Loss Service or ancillary services from the transmission provider or a third party for the purpose of completing a transmission transaction is not a sale-for-resale of power by a QF transmission customer that would violate our QF rules."³

Selkirk is right that it would be unfair to interpret the new NYISO tariff requirements in a way that would preclude entry of QFs into the new markets offered by the NYISO. The new competitive wholesale electric marketplace will require modest adjustments to policy determinations to account for the new institutions now offering services. In these situations, it is unlikely that precedent set in a prior regulatory framework will squarely match the facts surrounding issues that arise in the new regime. It would make little sense to design a new market, approve the mechanisms that will facilitate its operation, and, at the same time, rigidly apply precedent that was established under a different framework to the detriment of a particular set of participants. The arrangement here is identical to the one contemplated in Order 888-A in all relevant respects. If the determination has been made that arrangements by QFs for ancillary services from a transmission provider for purposes of completing a transmission transaction is not a sale-for-resale, then so too is the compliance by a QF with NYISO rules for energy imbalance service here not a sale for resale.

CONCLUSION

It is recommended that the question here certified be answered in the negative for three reasons: (1) this result is unopposed by any party; (2) in all relevant respects, that result is supported by the Commission's decisional rationale in Connecticut Valley; and (3) the result is consistent with the Commission's encouragement of open transmission access and competitive electric wholesale markets as determined in Order No. 888 and its progeny.

The following is certified to the Commission:

³ 62 Fed. Reg.12,274 at 12,310

1. The question appearing on the first page of this order;
2. Request of Selkirk Cogen Partners, L.P. that the Presiding Administrative Law Judge Certify a Question to the Commission, filed January 4, 2000, including the attached Memorandum in Support of Certified Question, as corrected and refiled on January 7, 2000;
3. Request of Lockport Energy Associates, L.P. that Presiding Administrative Law Judge Certify Question to the Commission, filed January 6, 2000;
4. Stenographic Transcript Pages 92-105 of the Prehearing Conference held on January 6, 2000;
5. Supplemental Memorandum of Selkirk Cogen Partners, L.P. and Lockport Energy Associates, L.P. filed January 20, 2000.

William J. Cowan
Presiding Administrative Law Judge

