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In order to facilitate an umbrella service agreement approach for short-term firm transmission service, minor modifications have been made to several sections of the pro forma tariff[FN390] as well as to Attachment A (Form of Service Agreement For Firm Point-To-Point Transmission Service). Notably, pages 3 and 4 of the service agreement, containing transaction specific information, is now required only for long-term firm point-to-point transmission service.

7. Other Tariff Provisions

a. Minimum and Maximum Service Periods

In the Final Rule, the Commission adopted a one-day minimum term for firm point-to-point service.[FN391] The Commission also concluded that it will not specify a maximum term for either firm point-to-point or network transmission service. However, the Commission modified the tariff to require that an application for transmission service specify the length of service being requested.

Rehearing Requests

CCEM states that a competitive market for hourly trades should be allowed to develop (transmission and ancillary services). It argues that contrary to the Commission's goal of comparability, the Rule effectively allows only incumbent utilities to participate in hourly markets on behalf of their own or network loads (citing section 13.1 of the pro forma tariff).

American Forest & Paper argues that firm and non-firm service should be made available on an hourly basis and that the Commission should assure that utilities make non-firm service available.

Commission Conclusion

It is unclear as to what hourly "trades" CCEM is referring. If CCEM is referring to off-system sales, the transmission provider is obligated to take transmission for any off-system sales under point-to-point transmission service under its tariff. Inasmuch as the tariff does not require the provision of hourly firm transmission, in order to provide itself with hourly firm transmission, the transmission provider would either: (1) reserve firm point-to-point service on a daily basis in order to participate in the hourly market or (2) propose in a section 205 filing to modify its tariff to voluntarily provide hourly firm point-to-point service. Under either circumstance, comparability would be maintained as all point-to-point customers would have equal access to the hourly market.

If CCEM is referring to purchases, hourly economy purchases by the transmission provider on behalf of its native load customers are also available on a comparable basis to network customers. However, if CCEM is referring to specific purchases made on behalf of a particular wholesale customer, this resale must be provided under point-to-point transmission service, as described above.

The Commission has rejected hourly firm point-to-point transmission service as a mandatory service to be provided under the Tariff.[FN392] Many entities would not oppose hourly firm service if afforded a lower priority, i.e., if they were curtailed before longer-term firm services. However, with this lower priority there may be little or no difference between the pro forma tariff non-firm service and curtailable firm hourly service. The Commission adopted the one-day minimum term for firm service to address concerns that customers would engage in "cream skimming" by taking firm service only during the hours at the daily peak while taking non-firm service for other hours, and thereby avoiding paying a fair share of the costs of the transmission system. However, this does not mean that the Commission would not allow such services if voluntarily proposed by a transmission provider.

Finally, in response to American Forest & Paper, the transmission provider has every incentive to make non-firm service available to all eligible customers in order to benefit native load customers, as the revenues generated by this service are typically used as a revenue credit to offset the costs of providing firm service. In addition, parties may raise concerns with the

Commission in a section 206 complaint if the transmission provider offers non-firm transmission service in a non-comparable, i.e., unduly discriminatory fashion.

b. Amount of Designated Network Resources

In the Final Rule, the Commission indicated that it will not change the limitation on the amount of resources a network customer may designate. [FN393] The Commission explained that a transmission provider is required to designate its resources and is subject to the same limitations required of any other network customer.

The Commission further explained that limiting the amount of resources to those that the customer owns or commits to purchase will protect a utility from having to incur costs that are out of proportion to the customer's load.

With respect to the allocation of interface capacity under network service, the Commission clarified that a customer is not limited to a load ratio percentage of available transmission capacity at every interface. It explained that a customer may designate a single interface or any combination of interface capacity to serve its entire load, provided that the designation does not exceed its total load.

Rehearing Requests

A number of entities state that section 30.8 of the pro forma tariff should be clarified to conform to the Final Rule preamble. The preamble states that a network customer should not be limited to a load ratio percentage of available transmission capacity at every interface, but may designate a single interface or any combination of interface capacity to serve its entire load, provided that the designation does not exceed its total load. However, they point out that section 30.8 of the pro forma tariff provides that a network customer's use of the transmission provider's total interface capacity with other transmission systems may not exceed the network customer's load ratio share.[FN394]

TAPS and Wisconsin Municipals ask the Commission to clarify the inconsistency by deleting the phrase "Ratio Share" at the end of the section 30.8. TAPS argues that section 30.8 of ***12349** the tariff conflicts with the preamble, other sections of the tariff itself (see section 28), and recent Commission orders (Wisconsin Public Service Corporation, 74 FERC 61,022 at 61,064 and FMPA v. FPL, 67 FERC 61,167 at 61,484). It further argues that load ratio restrictions on total interface usage would expand the market power of transmission providers.

EEI and Southern state that under section 30.8 and the related preamble language, it is unclear how the concept of load ratio share should be applied in the context of interface capacity, (i.e., is the network customer entitled to a load ratio share of available transmission capacity or total transmission capacity for an interface?). They argue that ATC is the appropriate basis for calculating shares of interface capacity and state that the Commission should specify that network service entitles the user to a load ratio share of the available capacity of each interface. EEI adds that if sufficient interface capacity is available, a request by a network customer to use available interface capacity to bring in resources for network load in excess of its load ratio share of the interface should be accommodated under the point-to-point tariff and treated on a first-come, first-served basis.[FN395]

Florida Power Corp states that "[i]n order to clarify that network customers may obtain transmission service over the transmission provider's interfaces in excess of their load ratio shares, the Commission should clarify that additional interface capability may be purchased (subject to availability) as firm point-to-point transmission service." (Florida Power Corp at 29).

Commission Conclusion

We agree that the pro forma tariff should be conformed to the preamble language in the Final Rule so that the interface capacity is limited to the customer's total load, not a load ratio share. This is consistent with the Commission's recent rehearing order in FMPA v. FPL:

We clarify that the phrase "that is, up to its share of the load, 3%" was not intended to limit FMPA's use of each interface to a discrete ratio (3%). Rather, FMPA, as well as Florida Power, can use each interface, if capacity is available, to service its entire network load. If the interface is [constrained] [sic], they will either pay redispatch costs or expansion costs based on their load ratio share.[FN[396]]

c. Eligibility Requirements

In the Final Rule, the Commission found that a non-discriminatory open access transmission tariff must be made available, at a minimum, to any entity that can request transmission services under section 211 and to foreign entities. [FN397]

Rehearing Requests

VT DPS and Valero state that the Final Rule does not appear to contemplate that marketers will buy network service or that one network service customer might serve a portion of the requirements of another network customer. Thus, they argue that network load can be double counted. To resolve this problem, they argue, service should be made available to suppliers rather than load, as provided in the NorAm NIS tariff, Section 1.5.

Commission Conclusion

Power marketers are specifically named in the definition of Eligible Customer (Section 1.11), and nothing in the Network Integration Transmission Service prohibits marketers from serving customers and designating those customers' loads (or portions thereof) as the marketers' Network Loads.

Additional rehearing requests regarding eligibility are addressed in Section IV.C.1. (Eligibility to Receive Non-discriminatory Open Access Transmission).

d. Two-Year Notice of Termination Provision

In the Final Rule, the Commission deleted the notice of termination provision from the tariff.[FN398]

Rehearing Requests

No requests for rehearing addressed this matter.

e. Termination of Service for Failure to Pay Bill

In the Final Rule, the Commission stated that section 7.3 of the Final Rule pro forma tariff provides that in the event of a customer default, the transmission provider may, in accordance with Commission policy, file and initiate a proceeding with the Commission to terminate service.[FN399]

Rehearing Requests

El Paso asserts that the Commission does not have the authority to prohibit a transmission provider from terminating service to a customer that has failed to pay its bill until permission from the Commission has been obtained. It argues that the Commission does not have abandonment authority under the FPA.

Commission Conclusion

El Paso is not correct. Under section 205 of the FPA, public utilities are allowed to effectuate changes in rates, charges, classification or service only after providing 60 days notice to the Commission and the public. Because a termination of service is clearly a change in service, public utilities must file notice of a termination 60 days prior to the proposed effective date.

In Portland General Electric Company, 75 FERC 61,310, reh'g denied, 77 FERC 61,171 (1996), we denied a requested waiver of section 35.15 of the Commission's Rules of Practice and Procedure to permit the utility to terminate service in the event of customer default. We indicated that we had previously explained the reasons for requiring public utilities to file notices of termination when seeking to discontinue service [FN400] and further explained that

Electricity is not just any commercial good or service. Rather, Congress in the Federal Power Act has charged us with ensuring that sales for resale or transmission of electricity in interstate commerce by public utilities take place at rates, terms and conditions that are just and reasonable.[FN[401]]

f. Definition of Native Load Customers

The Commission defined the term "Native Load Customers" in section 1.19 of the pro forma tariff as:

The wholesale and retail power customers of the Transmission Provider on whose behalf the Transmission Provider, by statute, franchise, regulatory requirement, or contract, has undertaken an obligation to construct and operate the Transmission Provider's system to meet the reliable electric needs of such customers.

Rehearing Requests

The pro forma tariff defines native load customers as "[t]he wholesale and retail power customers of the Transmission Provider. * * *" Cooperative Power argues that the definition of native load customers should recognize that joint planning is a sufficient criterion, and that construction and operation by the ***12350** transmission provider should not be necessary for native load status to be conferred. It asserts that under joint planning, the loads of transmission-only customers are considered native, therefore the Commission should eliminate the word power from the definition.[FN402]

NRECA and TDU Systems state that traditional wholesale customers that have long been on the system, have assisted in paying for past expansions, and will likely continue to be captive to a provider's monopoly transmission service, should have "native load equivalent" rights if they take network or long-term firm service. If the transmission provider has planned and will plan in the future for a customer's full or partial needs, they argue that the customer should be treated as the equivalent of native load. They point out that section 1.19 of the tariff limits native load status only to wholesale power customers of the transmission provider.

VA Com argues that the definition of native load in section 1.19 of the tariff should include existing distribution cooperatives and others who currently provide service to end users.

Commission Conclusion

We reject Cooperative Power's suggestion to include transmission-only point-to-point customers in the definition of native load. We note that network customers are provided with rights comparable to native load customers because the transmission provider includes their network resources and loads in its long-term planning horizon. However, a point-to-point transmission service customer is not similarly situated to native load and Network Customers. The Network service formula rate requires the Network customer to pay a load-ratio share of the costs of the transmission provider's transmission system on an ongoing basis, while a point-to-point transmission service customer is only responsible for paying on a contract demand basis over the contract term. The network customer and the native load of the transmission provider pay all the residual costs of the transmission system and face greater risks of rate fluctuations due to facility additions and variations in load of both its and other customers. In contrast, the point-to-point transmission service customer may be more transitory in nature electing shorter terms of service and specific forms of service tailored for discrete services over specific time periods that do not necessarily enter into the transmission provider's planning horizon. To the extent a transmission customer desires similar rights and cost responsibilities to a native load customer, it can always elect to take network service.

We further note that, in granting a right of first refusal to existing customers, we afforded existing transmission only point-to-point customers a priority to continue to use the transmission provider's system.

VA Com's proposed change to the definition of native load was made in conjunction with its proposed change in the reservation priority (highest priority for "native load", followed by firm contract customers and lastly, non-firm customers). Because we are rejecting VA Com's proposed reservation priority (see Section IV.G.3.a. above), we will also reject its proposed conforming change to the definition of native load as proposed by VA Com.

g. Off-System Sales

Regarding the unbundling of off-system sales, the Final Rule required that all bilateral economy energy coordination contracts executed before the effective date of Order No. 888 must be modified to require unbundling of any economy energy transaction occurring after December 31, 1996.[FN403] Concerning the treatment of revenues from transmission associated with off-system sales, the Commission stated in the Final Rule that revenue from non-firm services should continue to be reflected as a revenue credit in the derivation of firm transmission tariff rates.[FN404]

Rehearing Requests

Montana Power asserts that the Commission should clarify that off-system sales that originate from generating plants or power purchases outside the transmission provider's system and do not use the transmission provider's transmission system should not be automatically assessed point-to-point charges.

Maine Public Service asks the Commission to clarify that revenues from off-system sales are not to be credited where the sales do not use the transmission provider's system (referencing sections 1.44 and 8.1 of the pro forma tariff). Maine Public Service states that it makes sales from Maine Yankee (which is not located on Maine Public Service's system) to customers not on its system and that it should not have to credit these sales revenues to its transmission customers.

Wisconsin Municipals asks the Commission to clarify that the provision and level of revenue credits are rate issues and that if parties have negotiated provisions for revenue credits, the Final Rule cannot be used to avoid obligations undertaken in a settlement.

Commission Conclusion

Utilities must take all transmission services for wholesale sales under new requirements contracts and new coordination services under the same tariff used by eligible customers. The Commission provided an extension until December 31, 1996, for utilities to take transmission service under the same tariff for their economy energy transactions, certain power pooling arrangements, and other multi-lateral arrangements.[FN405] The above criteria, however, only apply when a utility transmission system is being used to accommodate off-system sales. Therefore, a utility would not be required to take point-to-point transmission service if its transmission system is not being used for the transaction.

Maine Public Service's concern is misplaced. Maine Public Service states that certain of its sales do not use its own transmission system and that it pays other utilities for such transmission service. However, Section 8.1 only specifies the treatment of revenues the transmission provider receives from transmission service it provides itself when making third-party sales using point-to-point transmission service under its tariff. If Maine Public Service is not the transmission provider for these third-party sales, then Section 8.1 does not apply to such transactions.

Wisconsin Municipals' argument with respect to prior settlements has been previously addressed in Section IV.D.1.c.(2) (Energy Imbalance Bandwidth).

h. Requirements Agreements

A detailed description of the Commission's unbundling requirements pertaining to requirements agreements is described below.

Rehearing Requests

Blue Ridge requests that the Commission clarify the definitions of requirements, economy and non-economy energy coordination agreements. In addition, Blue Ridge ***12351** seeks clarification regarding which dates are to be used to distinguish between existing and new contracts (July 11, 1994 or July 9, 1996).

Commission Conclusion

The definitions of economy and non-economy energy coordination agreements are addressed in section IV.F.4. (Bilateral Coordination Arrangements). With respect to Blue Ridge's concern regarding requirements agreements, we defined requirements contracts broadly in section 35.28(b)(1) of the Commission's regulations as "any contract or rate schedule under which a public utility provides any portion of a customer's bundled wholesale power requirements." The definition is intended to encompass partial requirements service, since that service is intended to meet the bundled load requirements of a customer that is not provided from other sources such as self-generation or unit power purchases. In contrast, a non-economy energy coordination agreement is not intended to meet, by itself, the entirety of a customer's bundled power requirement or the residual partial power requirement of a customer. For example, a 50 MW unit power purchase or a long-term firm power purchase would supply long-term firm power but a customer would likely need an additional partial requirements agreement to supply the residual amount of its load requirement.

Regarding Blue Ridge's request for clarification of the dates for new and existing agreements, the Commission explicitly stated in Order No. 888 that any bilateral wholesale coordination agreements executed after July 9, 1996 would be subject to the functional unbundling and open access requirements set forth in the Rule.[FN406] In addition, the Commission required that all bilateral economy energy coordination contracts executed on or before July 9, 1996 be modified to require unbundling of any economy energy transaction occurring after December 31, 1996. The Commission permitted all non-economy energy bilateral coordination agreements executed before July 9, 1996 to continue in effect subject to section 206 complaints.

For the purpose of distinguishing between existing and new wholesale requirements contracts and for stranded investment recovery provisions, the Commission established July 11, 1994 as the applicable date.[FN407] For a utility to recover stranded investment costs in new requirements contracts, it must include explicit provisions in the contract for stranded investment recovery. Existing requirements contracts would not need a similar provision to be eligible for stranded investment recovery. [FN408] Utilities are required to unbundle all new requirements contracts. The requirement that utilities unbundle existing wholesale requirements contracts is for informational purposes and will enable existing requirements customers to evaluate and compare the transmission component of existing contracts to alternative contracts prior to the existing contracts' expiration dates.

i. Use of Distribution Facilities

The Commission received requests for clarification regarding this issue which was not specifically addressed by the Commission in the Final Rule.

Rehearing Requests

CSW Operating Companies asks the Commission to make clear that to the extent a transmission provider makes available to transmission customers the use of distribution facilities, the terms governing the use of and the charges for such use should be set forth in the customer's service agreement.

Commission Conclusion

Utilities are free to include customer-specific terms and conditions or terms and conditions limited to certain customers (e.g., a distribution charge) in a customer's service agreement and/or the network customer's network operating agreement.

j. Losses

The Commission received requests for clarification regarding this issue which was not specifically addressed by the Commission in the Final Rule.

Rehearing Requests

VT DPS asserts that network customers should not have to bear losses twice—the tariffs allow collection of losses over all network load, even that supplied by behind the meter generation. It argues that losses should only be paid on power actually transmitted over the company's system.

Commission Conclusion

The pro forma tariff neither specifies the applicable Real Power Loss factors (see tariff section 28.5) nor the demand levels to which the loss factors should be applied. Accordingly, concerns regarding the loss calculation for a customer should be raised when the transmission provider files with the Commission a service agreement for a network customer.

k. Modification of Non-Rate Terms and Conditions

The Commission's requirements pertaining to modification of non-rate terms and conditions is described below.

Rehearing Requests

TAPS asserts that the language of section 35.28(c)(1)(v) and the preamble of Order No. 888 are inconsistent. TAPS argues that the Commission should require a demonstration of consistency with and superiority to the terms and conditions of the pro forma tariff and indicate that it will not allow deviations that seek to withdraw the minimum terms and conditions of non-discriminatory transmission. According to TAPS, the Commission should also clarify that the Commission will not let onerous tariff terms creep in through the back door, i.e., through service agreements. TAPS also maintains that the Commission should not allow transmission providers to use conformity as an excuse to evade commitments.

Commission Conclusion

Order No. 888 allows a utility the flexibility to propose, after the compliance tariffs go into effect, to modify non-rate terms and conditions of the tariff if it can "demonstrate[] that such terms * * * are consistent with, or superior to, those in the compliance tariff." These are the same principles that are referenced in the regulation language (deviations allowed if the transmission provider can demonstrate the deviation is consistent with the principles of Order No. 888). While utilities are free to file revised tariffs after their compliance filings, any filing including service agreements will be carefully reviewed by the Commission to assure that the revised tariffs and service agreements are just and reasonable and consistent with the principles of Order No. 888.

With regard to TAPS' concern about transmission providers evading commitments, we reiterate that we will not require abrogation of existing contracts (and the commitments reflected therein) except on a case-specific basis.

l. Miscellaneous Tariff Modifications

(1) Ancillary Services

The Commission explained that the pro forma tariff incorporates conforming revisions consistent with the ***12352** determinations discussed in the Final Rule.[FN409]

(2) Clarification of Accounting Issues

In the Final Rule, the Commission offered clarifications on the Final Rule pro forma tariff requirements and certain other accounting issues related to the Final Rule.[FN410]

(a) Transmission Provider's Use of Its System (Charging Yourself)

In the Final Rule, the Commission stated that the purpose of functional unbundling is to separate the transmission component of all new transactions occurring under the Final Rule pro forma tariff, thereby assisting in the verification of a transmission provider's compliance with the comparability requirement. With respect to off-system sales, the Commission stated that the transmission provider would book to operating revenue accounts those revenues received from the customer to whom it made the off-system sale.[FN411] The Commission required that the transmission service component and energy component of those revenues be recorded in separate subaccounts of Account 447, Sales for Resale.

Rehearing Requests

APPA argues that the revenue from the transmission component of all off-system uses must be included in the credit if comparability is to be achieved.

APPA also argues that booking revenue credits to Account 447 for a test year reduction does not ensure timely receipt by customers. It asserts that a monthly pass-through to all firm transmission customers is needed.

APPA further argues that a properly functioning revenue credit does away with the perception of disparate treatment of network and point-to-point customers. Similarly, TDU Systems argues that comparability requires that revenues attributable to transmission owners' use of their transmission systems be flowed through to customers' benefit immediately so that transmission owners and customers receive comparable price signals with regard to their uses of the system.

Commission Conclusion

The precise methodology to be used to credit revenues from off-system sales for the benefit of the tariff customers should be addressed in the compliance filing proceedings and will depend on the particular rate design methodology that is ultimately employed. APPA's proposed monthly pass-through of revenue credits raises potential issues including: (1) use of estimates versus actuals; (2) the appropriate time period to be utilized; and (3) firm versus non-firm distinctions. Accordingly, the issue of determining appropriate revenue credits is properly left for case-by-case determinations. However, we agree with APPA that revenue from the transmission component of all off-system uses of the transmission system (whether by the transmission provider or a transmission customer) must be treated on a comparable basis, whether through rate design or through revenue credits.

(b) Facilities and System Impact Studies

In the Final Rule, the Commission explained that comparability mandates that to the extent a transmission provider charges transmission customers for the costs of performing specific facilities studies or system impact studies related to a service request, the transmission provider also must separately record the costs associated with specific studies undertaken on behalf of its own native load customers, or, for example, for making an off-system sale.[FN412]

Rehearing Requests

No requests for rehearing addressed this matter.

(c) Ancillary Services
In the Final Rule, the Commission indicated that, at this time, it was not convinced that the amounts involved or the difficulty associated with measuring the cost of ancillary services warrants a departure from our present accounting requirements.[FN413]

Rehearing Requests
No requests for rehearing addressed this matter.

(3) Miscellaneous Clarifications

(a) Electronic Format
In the Final Rule, the Commission required that public utilities, in addition to complying with the requirements of Part 35, submit a complete electronic version of all transmission tariffs and service agreements in a word processor format, with the diskette labeled as to the format (including version) used, initially and each time changes are filed.[FN414]

Rehearing Requests
No requests for rehearing addressed this matter.

(b) Administrative Changes
In the Final Rule, the Commission set forth a number of tariff modifications that it indicated needed no further explanation. [FN415]

8. Specific Tariff Provisions
The Commission attached a pro forma tariff to the Final Rule as Appendix D. A number of entities have sought rehearing of various sections of that pro forma tariff. Their arguments and the Commission's responses are set forth below.

Rehearing Requests
Oklahoma G&E asks that the Commission add a definition for "Interconnection" that would be an interface where one or more points of delivery or points of receipt are located.

Commission Conclusion
We disagree with Oklahoma G&E that there is a need to add a definition for "Interconnection" to the Final Rule pro forma tariff. Oklahoma G&E has not supported its need for the proposed change and has failed to identify any potential problems that may result if its definition is not included.

Sections 1.12, 15.4 and 32.4

Rehearing Requests
Cajun argues that the Commission should mandate joint planning in the development of Facilities Studies. It alleges that a transmission provider's independent long-range plans frequently include longer, higher voltage facilities than are needed for the transmission customers' requirements. It further alleges that absent mandatory joint transmission planning, the transmission customers will always be paying for the incremental capacity cost of transmission enhancements that only fit into the Transmission Provider's independent long-range plans.

Commission Conclusion
A joint planning mandate as recommended by Cajun, NRECA and others is beyond the scope of this proceeding. However, the Commission encourages utilities to engage in joint planning with other utilities and customers and to allow affected customers to participate in facilities studies to the extent practicable. Moreover, on a regional basis, the Commission encourages the formation ***12353** of RTGs and ISOs to represent the needs of all participants in a region in the planning process.

Section 1.14

Rehearing Requests
CCEM asserts that the term Good Utility Practice is vague. It argues that the Commission should delete the reference to regional practices, but if it does not, the term should be clearly defined in each utility's tariff.

Commission Conclusion
The Commission recognizes that unique operating practices and conditions exist on a regional basis throughout the industry. Accordingly, the Commission permits certain deviations to the non-price terms and conditions of the tariff. In the Final Rule, we stated that any proposed modifications by the utility to the tariff to recognize regional operations and practices must be demonstrated to be reasonable, generally accepted in the region, and consistently adhered to by the transmission provider. [FN416]

Sections 1.22 and 1.25

Rehearing Requests
Blue Ridge requests clarification that a portion of a designated network resource need not consist of the entirety of a generating unit.

Commission Conclusion
Blue Ridge's request for clarification in the definition of "Network Load" in Tariff Section 1.22 and "Network Resource" in Tariff Section 1.25 is not necessary. Blue Ridge's concerns are based on the mistaken premise that a designated network resource must consist of the entirety of a generating unit. Tariff sections 1.25 and 30.1 explicitly specify that a network resource can be a portion of a generating resource or unit. Indeed, the Commission recently emphasized this point:

Ohio Cooperatives have disregarded the fact that a designated resource can be a part of a unit. In this example, Ohio Cooperatives would make two network designations for the 300 MW unit: a 100 MW designation for the 100 MW load on one system and a 200 MW designation for the 200 MW on the other system.[FN417]

Sections 1.25 and 30.1

Rehearing Requests
TDU Systems asserts that these sections should not be read to require assignment of specific Network Resources to specific control areas. They state that multiple control area network customers need to be able to dispatch their resources economically to serve their loads. They argue that the Commission would be in error to require that a transmission customer's resources be segmented if they are being dispatched to serve network load in one of several control areas and once so segmented, sales from such units be considered either third-party sales or become interruptible as to network load in a second control area and thus are not deemed Network Resources. They further argue that TDU systems with loads and resources in multiple control areas must be allowed to designate as Network Resources for each control area the totality of their resources which meet the owned or purchased requirements of section 1.25.

TDU Systems argues that these sections should be revised to include resources that are leased by a network customer on terms tantamount to ownership, or which, at a minimum, afford the network customer a first call right to that generating resource.

Commission Conclusion
TDU Systems' proposed revision to recognize leased resources appears reasonable and we revise these sections of the pro forma tariff, in relevant part, as follows (new text underlined, deleted text in brackets):

1.25 Network Resource: Any designated generating resource owned, [or] purchased or leased by a Network Customer under the Network Integration Transmission Service Tariff.

30.1 Designation of Network Resources: Network Resources shall include all generation owned, [or] purchased or leased by the Network Customer designated to serve Network Load under the Tariff.

Sections 1.33 and 1.34

Rehearing Requests
CCEM states that sections 1.33 and 1.34 should be changed to facilitate umbrella service agreements that include all points of receipt and delivery on a transmission provider's system.

Commission Conclusion
Consistent with our ruling in section IV.G.6 (Umbrella Service Agreement) regarding umbrella type service agreements for short-term firm point-to-point transmission service, we will modify sections 1.33 and 1.34 to require that Points of Receipt and Points of Delivery be specified in the service agreement for only Long-Term (more than one year) Firm Point-to-Point Transmission service.

Section 1.47

Rehearing Requests
Wisconsin Municipals asks the Commission to clarify that a utility is not prevented from including the load of interruptible customers in the denominator of the fraction used to perform the load ratio calculation. It claims that this is important in Wisconsin where the transmission system is planned without regard to the distinction between firm and interruptible power customers (interruptible customers are not subject to interruption for transmission reasons).

Commission Conclusion
The treatment of interruptible loads in the planning and operation of the Wisconsin transmission grid present a unique, case-specific situation that is best addressed on a case-by-case basis. As the Commission stated in the Final Rule:

all tariffs need not be "cookie-cutter" copies of the Final Rule tariff. Thus, under our new procedure, ultimately a tariff may go beyond the minimum elements in the Final Rule pro forma tariff or may account for regional, local, or system-specific factors. The tariffs that go into effect 60 days after publication of this Rule in the Federal Register will be identical to the Final Rule pro forma tariff; however, public utilities then will be free to file under section 205 to revise the tariffs, and customers will be free to pursue changes under section 206.[FN[418]]

Section 1.48

Rehearing Requests
Oklahoma G&E asks the Commission to clarify that the term "Transmission Service" as used in the pro forma tariff includes service provided on a network basis as well as on a point-to-point basis.

Commission Conclusion
The Commission used the term "Transmission Service" throughout the pro forma tariff to refer only to point-to-point service and not network service. We also note that the term "transmission service" (in lower case), which is also used throughout the pro ***12354** forma tariff, was used to refer to both point-to-point and network service. Oklahoma G&E has not identified any problems associated with our use of these terms and therefore has not supported its proposed modification.

Section 1.49

Rehearing Requests
Santa Clara and Redding state that the transmission system is defined as facilities owned, controlled or operated and that this could result in the same transmission facilities being the part of the transmission system of two entities (e.g., COTP, which is owned by TANC, but operated by Western Area Power Administration (WAPA)). They ask the Commission to clarify that only one such entity should have the obligation to provide transmission service.

Commission Conclusion
This presents a fact-specific situation that is best addressed on a case-by-case basis. This situation would appear to arise for WAPA and TANC only if either utility receives a request for reciprocal transmission service or if either utility files a voluntary tariff. The appropriate entity to include the COTP facility in its transmission system for purposes of a transmission tariff may depend upon the circumstances of the transmission request. Therefore, a resolution of this question is appropriately deferred until such time as reciprocal service using the COTP facility is requested.

Section 3

Rehearing Requests
CCEM asks the Commission to clarify that a transmission customer may switch its supplier of ancillary services.

Commission Conclusion
The Final Rule requires that transmission customers obtain all necessary ancillary services for their transactions. They must purchase certain of these services from the transmission provider, but can self supply or obtain certain services from a third party. Consistent with these requirements, a transmission customer may switch suppliers of ancillary services not required to be provided by the transmission provider if it continues to demonstrate that it satisfies its ancillary service obligations.

Section 5.1

Rehearing Requests
ConEd points out that this section applies to Transmission Service, which the tariff defines to mean point-to-point service only. It requests that this section be clarified to include network service.

Commission Conclusion

The use of the term "Transmission Service" in section 5.1 of the pro forma tariff was an inadvertent error. We will change the term "Transmission Service" used in section 5.1 to "transmission service" so as to include both point-to-point and network transmission service.

Section 6

Rehearing Requests
CCEM asks the Commission to require that the text of the required sworn statement by non-transmission owning entities that they are not assisting an Eligible Customer be included in the tariff.

Commission Conclusion
We will deny CCEM's request as unnecessary. The Commission does not believe that it must mandate the precise text of the required sworn statement. Rather, the entity requesting transmission service properly has the burden of explaining in a sworn statement the circumstances of its service request, including on whose behalf it may be requesting service (for itself or for another party).

Section 8

Rehearing Requests
CCEM argues that, consistent with Commission policy for natural gas pipelines, transmission providers should be required to refund all "penalties" that are in excess of the costs incurred to balance transmitting system operations (citing Transco, 55 FERC 61,446 at 62,372 (1991) and TETCO, 62 FERC 61,015 at 61,117 (1993)).

Commission Conclusion
CCEM's argument is premature. Order No. 888 did not establish a rate or a penalty for Energy Imbalance Service. CCEM is free to raise this concern at such time as utilities file their proposed rates for Energy Imbalance Service.

Section 11

Rehearing Requests
CCEM contends that an unconditional and irrevocable letter of credit is extremely costly to obtain and could be used as subterfuge for discriminatorily denying service. CCEM argues that if an irrevocable letter of credit is used, a transmission provider should not be able to draw on it until it tenders a bill that has been improperly refused. (CCEM attached a proposed conditional letter of credit to its rehearing request). Several entities argue that a letter of credit should not be required for existing customers with a satisfactory credit history and should only apply to new customers or those with a history of payment delinquency.[FN419]

Commission Conclusion
While a transmission provider may require an unconditional and irrevocable letter of credit, if a customer believes that the transmission provider unreasonably rejected an alternative security proposal, it may seek relief through the dispute resolution procedures established in Tariff Section 12. Moreover, if a customer believes a transmission provider is attempting to use the unconditional and irrevocable letter of credit in an unduly discriminatory manner, it may file a complaint raising such concern in a section 206 filing.

Section 12

Rehearing Requests
According to Public Service Co of CO, the dispute resolution procedures: (1) Should allow a party to appeal an arbitration award on the basis that arbitrators have misinterpreted the requirements of the pro forma tariff and (2) where a utility is a member of an RTG, should allow the RTG dispute resolution procedures to be exclusive. Otherwise, Public Service Co of CO argues, entities may perceive that the Commission's procedures are more favorable than the RTG's and decide not to join. Moreover, it asserts that when a utility that is a member of an RTG has a dispute with a customer that is a non-member, the customer's forum should be the Commission, or the RTG's procedures if those procedures apply to non-members.

Dispute Resolution Associates asks the Commission to require that prior to submission of disputes for arbitration or Commission disposition, disputants should be required to pursue a mediated resolution with a qualified individual. If unsuccessful, it states that parties can elect arbitration or Commission disposition. If successful, it states that parties will have avoided litigation related costs and will not have jeopardized their ongoing business relationship. Dispute Resolution Associates also argues that representatives at all negotiating sessions should be authorized to enter into an agreement and asks that the Commission clarify that dispute resolution is one of the minimum requirements of the Final Rule. It also asks that the Commission require that any filed separate retail transmission ***12355** tariffs must include section 12 type dispute resolution procedures.

Commission Conclusion
Concerning the first issue raised by Public Service Co of CO, even if the arbitrator misinterprets the requirements of the pro forma tariff, the dispute resolution procedures require such decision (as it affects terms and conditions of service) to be filed with the Commission. Section 12.2 provides:

The final decision of the arbitrator must also be filed with the Commission if it affects jurisdictional rates, terms and conditions of service or facilities.

As to Public Service Co of CO's second concern, a utility's membership in an RTG with its own Dispute Resolution Procedures presents a fact specific situation to which a generic response is not appropriate. Whether both parties to a dispute are members of the RTG or only one of the parties is a member may have some bearing on which set of Dispute Resolution Procedures should apply.

Regarding Dispute Resolution Associates concerns, a utility is free to propose an initial process using "mediated resolution with a qualified individual" prior to using the Dispute Resolution Procedures. However, we see no need to modify the tariff to introduce such a proposed requirement as the Commission is not aware of other parties similarly claiming excessive costs or the threat of "jeopardizing ongoing business relationship[s]" due to the present Dispute Resolution Procedures. Finally, any attempts to delete the Dispute Resolution Procedures from any tariff on file with the Commission would require the transmission provider to demonstrate that its proposed modifications are consistent with or superior to the pro forma tariff terms and conditions.

Section 13.2

Rehearing Requests
CCEM asserts that the term "reserved service" should be changed to "requested service." Utilities For Improved Transition and Florida Power Corp assert that the limitations on unconditional reservations are too stringent and that the Commission should modify the third sentence of section 13.2 to provide: "If the Transmission System becomes oversubscribed, requests for longer-term service may preempt requests for shorter-term service up to a time period before the requested commencement of service that is equal to the requested term of service."

Commission Conclusion

We will deny CCEM's request to replace the term "reserved service" in tariff section 13.2 with "requested service." CCEM has not attempted to identify any uncertainties caused by the current wording of this section or explain any improvements that its proposed change would make.

Utilities For Improved Transition and Florida Power Corp's proposal to revise the deadline for when reservations for short-term firm transmission become unconditional is contrary to the Commission's intent in adopting the conditional reservation approach for short-term firm transmission and is rejected. Specifically, for service requests greater than a single day, week or month, Utilities For Improved Transition and Florida Power Corp's proposal decreases the period of time that such request is conditional; in other words, such request increases the unconditional reservation period, thus reducing the amount of longer-term transactions that the transmission provider can accommodate.

Sections 13.2 and 14.2

Rehearing Requests

CCEM notes that short-term firm point-to-point transmission service customers that have already reserved service have a right to match any longer-term requests for service before being preempted pursuant to section 13.2. However, CCEM states that these tariff sections do not establish a deadline for when such right must be exercised. Because the tariff established a conditional reservation period for short-term firm transmission service (during which time longer-term firm transmission requests can preempt shorter-term conditional reservations) CCEM suggests that a shorter-term firm transmission customer should be allowed to exercise its right to match longer-term service requests up until the end of the conditional reservation period. CCEM requests a similar clarification for non-firm transmission service but does not propose specific modification.

Commission Conclusion

While we agree with CCEM regarding the need to establish a deadline for exercising the right to match longer-term service requests for both short-term firm and non-firm transmission services, we will reject CCEM's proposed deadline for short-term firm transmission service. CCEM's proposed deadline would create market inefficiency by allowing the holder of the shorter-term firm transmission service an excessive amount of time to exercise its right to match the longer-term service. We feel that such a proposal could constitute a form of hoarding that would stifle the consummation of potential transactions and should not be allowed. CCEM's proposal would work to the detriment of any and all potential customer(s) requesting longer short-term firm transmission service. By allowing the original transmission customer to delay its response, the subsequent potential customer will be disadvantaged and may be required to make last minute alternative arrangements.

We believe that an especially quick response time is necessary for hourly non-firm transmission service customers to match longer-term service requests. Hourly non-firm transmission customers must exercise their right to match longer-term service requests immediately upon notification by the transmission provider of a longer-term competing request for non-firm transmission service. For non-firm transmission service other than hourly transactions and short-term firm transmission service, we believe a customer should exercise its right to match longer-term service requests as soon as practicable. The prompt exercising of such right is particularly critical where scheduling deadlines for such transactions are imminent. However, even for transactions with longer lead-times before service is to commence, we believe a response deadline of no more than 24 hours from being informed by the transmission provider of a longer-term competing request for transmission service is appropriate. Accordingly, the customer will be required to respond to the transmission provider as soon as practicable after notification of a longer-term request for service, but no longer than 24 hours from being notified or earlier if required to comply with the scheduling requirements for such services in tariff section 13.8 and 14.6. Tariff sections 13.2 and 14.2 will be modified accordingly.

Section 13.5

Rehearing Requests

Several utilities argue that section 13.5 is too broad because it also applies to costs that are included in rates on an embedded cost basis (which they claim can be evaluated when the transmission provider makes a rate filing).[FN420] They recommend that the Commission ***12356** modify the last sentence of the section as follows:

If redispatch costs or Network Upgrade costs are to be charged to the Transmission Customer on an incremental basis or costs relating to Direct Assignment Facilities that are to be charged to the Transmission Customer, the obligation of the customer to pay such costs shall be specified in the Service Agreement prior to the initiation of service." (Utilities For Improved Transition at 74-75).

Commission Conclusion

The Commission's intent in tariff section 13.5 was to require that any proposal to assess incremental charges to a customer must be specified in that customer's service agreement. Florida Power Corp and VEPCO correctly note that tariff section 13.5 inadvertently requires that any redispatch, network upgrade or direct assignment facilities, whether assessed on an incremental basis or included in embedded cost rates, must be specified in a customer's service agreement. To eliminate this unintended result, tariff section 13.5 is revised in relevant part as follows (new text underlined):

Any redispatch, Network Upgrade or Direct Assignment Facilities costs to be charged to the Transmission Customer on an incremental basis under the Tariff will be specified in the Service Agreement prior to initiating service.

Section 13.6

Rehearing Requests

CCEM asserts that the term "Good Utility Practice" should be deleted. CCEM claims that the inclusion of regional practices in Good Utility Practice makes the phrase vague and unpredictable. CCEM proposes that the Commission replace this phrase with a qualifier that pertains only to reliability and safety. According to PA Coops, equal priority places inordinate and unwarranted pressure on state siting and regulatory authorities to approve transmission projects required to provide service that may primarily benefit out of state parties. NYSEG argues that the Commission is not authorized to require curtailment of bundled retail service because it does not have jurisdiction over the rates, terms, and conditions of such service. It asserts that transactions subject to proportional curtailment should not include a transmitting utility's own use of its system to transmit its owned and purchased generation to native load customers as part of bundled retail service or services under rate schedules that are grandfathered. For transactions subject to proportional curtailment, NYSEG argues that allocation of curtailments will be comparable only if those multiple transactions being curtailed are of the same type of service and if each of the multiple transactions is for the same duration—these curtailments should be made on the same basis as required for non-firm PTP service. It asks the Commission to clarify that the curtailment requirements are not applicable to existing transmission contracts.

Commission Conclusion

CCEM's concerns center on the inclusion of the phrase regional practices in the definition of Good Utility Practice in section 1.14 of the pro forma tariff. These concerns are answered in section 1.14 above.

PA Coops' argument that long-term firm point-to-point transmission customers should be curtailed before network service customers and native load ignores the fact that the transmission provider has an obligation under the pro forma tariff to expand or upgrade its transmission system in response to requests for such long-term point-to-point transmission requests. In turn, such long-term firm point-to-point transmission customers undertake an obligation to pay for any transmission facility additions necessary for the provision of service pursuant to the tariff. Comparability requires that all long-term firm transmission customer be treated on a not unduly discriminatory basis in terms of curtailment priority.

Regarding NYSEG's arguments, the purpose of the curtailment provisions of the pro forma tariff is not to "requir[e] curtailment of bundled retail service" as NYSEG claims. Rather, the provision simply requires the transmission provider to curtail network and point-to-point transmission services on a basis comparable to the curtailment of the transmission provider's service to its native load. Indeed, we have repeatedly indicated that we do not have jurisdiction over bundled retail sales.

NYSEG's concerns regarding curtailment provisions in existing contracts are addressed above in Section IV.G.3.a. (Pro-rata Curtailment Provisions).

Section 13.7

Rehearing Requests

Utilities For Improved Transition and Florida Power Corp state that section 13.7 of the pro forma tariff makes it uneconomic to engage in system sales transactions on a firm basis because it requires the transmission provider to impose a separate charge for transmission from each generating station. They ask that the Commission clarify that if there is a sale from multiple generators, a reservation of transmission from each point of receipt will be required only in the amount of the expected relative contribution of each generating station to the energy that is sold. If it is not so clarified, they argue that the Commission should make one of the following modifications: (1) permit the customer to designate more than one generating station as a single point of receipt if it provides likely loadings of the units to the transmission provider; (2) provide that where the customer takes service from a group of generating stations on an economic dispatch basis, the reserved capacity is the sum of the reservations at the points of delivery (must also provide likely loadings); or (3) add a new subsection to Article 31 that provides that a network integration transmission customer may also reserve service on a contract demand basis for periods as short as one day (but do not reduce the one-year minimum term for load-based network service).

CSW Operating Companies asserts that the Commission should permit sales of power from multiple points of receipt, but such multiple generating units should be considered a single point of receipt. According to CSW Operating Companies, this provides maximum flexibility, lessens the need to establish secondary points of receipt, and is consistent with FMPA v. FPL, 74 FERC 61,006 at 61,014 (1996). They ask that the Commission revise section 13.7(b) to provide: "The Transmission Customer may purchase transmission service to make sales of capacity and energy from multiple generating units that are on the Transmission Provider's Transmission System. Such multiple generating units shall be considered a single Point of Receipt when the underlying sale is to be made on a system basis and not from specific generating units." (CSW Operating Companies at 10-11). TAPS requests that the Commission clarify that a network customer may make system sales to third parties using the point-to-point provisions without designating each generating resource as a point of receipt. Moreover, it asks that if the Commission intends to depart from FMPA v. FPL, that transmission providers be held to the same burden.

Commission Conclusion

Several utilities request rehearing on the tariff's requirement that sales of capacity and energy from multiple generating units must be designated as multiple points of receipt under point-to-point transmission service. These parties generally claim that this tariff requirement makes system sales ***12357** transactions uneconomical and is contrary to the Commission's determination in FMPA v. FPL, 74 FERC 61,006 at 61,014 (1996).

As the Commission stated in the Final Rule:

all tariffs need not be "cookie-cutter" copies of the Final Rule tariff. Thus, under our new procedure, ultimately a tariff may go beyond the minimum elements in the Final Rule pro forma tariff or may account for regional, local, or system-specific factors. The tariffs that go into effect 60 days after publication of this Rule in the Federal Register will be identical to the Final Rule pro forma tariff; however, public utilities then will be free to file under section 205 to revise the tariffs, and customers will be free to pursue changes under section 206.[FN[421]]

Utilities that advocate modifying the pro forma tariff to accommodate system sales are free to file their specific proposals with the Commission in a section 205 filing.[FN422] Such proposals are best reviewed on a case-specific basis where the type of system sales engaged in by the transmission provider or transmission customer can be identified and described in detail. In order to ensure comparability, any proposed tariff modifications submitted in order to facilitate system sales of the transmission provider must also apply for sales by transmission customers as well.

Section 13.7(b)

Rehearing Requests

Blue Ridge argues that because units at the same geographic location can be connected to the system at different electrical locations, such as connections at different voltage levels (e.g., one unit connected at 500 kV and another unit connected at 230 kV), the Commission should replace the phrase "at the same generating plant" with "at the same electrical location." (Blue Ridge at 23-24).

Commission Conclusion

Blue Ridge's proposed change is unsupported. The rationale supporting the need for such change and its intended result is unclear and unexplained and appears to be unnecessary and overly restrictive. Many generating units at a single plant are connected to the transmission grid at multiple voltages. Therefore, taking Blue Ridge's proposal to its logical end, a customer could face an additional charge at a single unit for every voltage level connection. In contrast, the intent of section 13.7(b) of the pro forma tariff is to treat multiple units at a single plant as a single point of receipt to avoid charging a customer an unnecessary additional charge.

Section 13.8

Rehearing Requests

CCEM asks the Commission to clarify that permissible scheduling changes extend to changes in the amount of power scheduled, the generation source, and delivery and receipt points. AMP-Ohio asserts that if the transmission provider can accommodate a change, the customer should be able to change its schedule less than 20 minutes before the hour or during the hour, and during an emergency or when the customer is attempting to remain within the 1.5% deviation band. It also asks the Commission to clarify that customers should be allowed to aggregate multiple points of delivery of less than a whole megawatt to be stated in whole megawatts (as is allowed for points of receipt). Otherwise, AMP-Ohio asserts, this would preclude small utilities from receiving service under a transmission provider's open access tariff.

Commission Conclusion

We agree with CCEM that permissible scheduling changes include the amount of power scheduled (up to the amount of capacity reservation stated in the customer's service agreement). However, a proposed modification to the generation source or to receipt and delivery points on a firm basis under the pro forma tariff is not simply a scheduling change, as maintained by CCEM, but is a new request for service, as set forth in pro forma tariff section 22.2.

AMP-Ohio's request regarding scheduling changes ignores the optional language in section 13.8 of the pro forma tariff, which permits a reasonable time limitation (other than the stated twenty minute deadline) that is "generally accepted in the region and is consistently adhered to by the transmission provider." Accordingly, the pro forma tariff may be amended by the transmission provider to reflect the prevailing practice in the region.

AMP-Ohio's request regarding scheduling changes to allow the customer to stay within the deviation band of 1.5 percent may not be feasible depending upon the ramping rates of the particular generating units and may allow erratic scheduling by customers that could interfere with the transmission provider's ability to provide load following service.

AMP-Ohio's request for clarification that customers should be allowed to aggregate multiple points of delivery of less than a whole megawatt is unnecessary. Tariff section 17.2(viii) specifically allows customers to combine their requests for service for either points of receipt or points of delivery in order to satisfy the minimum transmission capacity requirement.

Section 14.2

Rehearing Requests

Tallahassee asks the Commission to clarify that a non-firm customer facing possible interruption for economic reasons will be allowed to match the duration and price of the surviving transaction and that once a non-firm transaction begins, it will not be preempted without whatever notice is sufficient and appropriate in the region, but the time period should be no shorter than 1-2 hours.

Commission Conclusion

The pro forma tariff does allow a customer to match a longer term reservation before being preempted. Moreover, non-firm transmission transactions, by definition, are interruptible for economic reasons (on a non-discriminatory basis) at any time. To the extent a prevailing regional practice exists regarding advance notice of interruption, the transmission provider may incorporate such a provision in its tariff.

Section 14.4

Rehearing Requests

CCEM asks the Commission to clarify that a non-firm point-to-point service agreement is an Umbrella Agreement and a non-firm point-to-point customer should be able to schedule a transaction at different primary and secondary receipt points and schedule changes in primary points with no filing requirement.

Commission Conclusion

The form of service agreement for non-firm transmission service is a non-transaction specific umbrella service agreement (See Attachment B to the pro forma tariff). Therefore, the service agreement does not require a specification of receipt and delivery points for non-firm point-to-point transmission service. However, we note that changes to the receipt or delivery points for non-firm transmission service other than those points reserved by the transmission customer in its service request are not "schedule" changes as claimed by CCEM, but will require the ***12358** submission of a new application for service pursuant to Tariff Section 18.

Section 14.6

Rehearing Requests

CCEM asks the Commission to clarify that "scheduling changes" for non-firm transmission include changes in the amounts scheduled, changes in receipt and delivery points, or changes in primary points.

Commission Conclusion

This issue is addressed in Section 13.8 above.

Sections 17, 18 and 29.2

Rehearing Requests
The EPRI/NERC Working Group (formerly the "What and How Industry Working Group") identifies certain areas in the pro forma tariff "where the perceived scope of OASIS has grown beyond that which is feasible in Phase 1" of OASIS. (EPRI/ NERC Working Group at 2). EPRI/NERC Working Group references various information required in the application process under the pro forma tariff that is required to be submitted via OASIS to the transmission provider. EPRI/NERC Working Group explains that a substantial amount of information required under the pro forma tariff "cannot be provided via the OASIS in Phase 1" (e.g., service agreements, requests for (A) non-firm point-to-point transmission service in the next hour, (B) multiple receipt and delivery points, (C) addition of new network loads or resources, loadflow and stability data).

The EPRI/NERC Working Group also claims that tariff section 17.1 creates confusion as it first requires that "[a] request for Firm Point-To-Point Transmission Service * * * must contain a written Application * * *" to the transmission provider, but then requires "[a]ll Firm Point-To-Point Transmission Service requests should be submitted by entering the information listed below on the Transmission Provider's OASIS." (Emphasis added). The EPRI/NERC Working Group asserts that the above language confuses the process of an "application for service agreement" versus the process of "a request for transmission service" by a customer who already has a service agreement.

Commission Conclusion
The Commission recognizes that implementation of the OASIS is being accomplished in phases. In recognition of this fact, section 17.1 of the pro forma tariff provides:

Prior to implementation of the Transmission Provider's OASIS, a Completed Application may be submitted by (i) transmitting the required information to the Transmission Provider by telefax, or (ii) providing the information by telephone over the Transmission Provider's time recorded telephone line.

Moreover, we clarify that if Phase 1 of OASIS implementation does not support the submission of certain information over the OASIS, such information may be submitted by telephone or telefax (facsimile), as provided in the pro forma tariff, and promptly (within one hour) posted on OASIS by the Transmission Provider.[FN423]
Concerning the EPRI/NERC Working Group's apparent confusion regarding service application processes, we previously explained in Section IV.G.6 that the Commission is modifying the application process for firm point-to-point transmission transaction of less than one year (short-term firm transactions). The Commission will permit an "umbrella service agreement" approach where all of a customer's short-term firm transactions can be arranged under a single non-transaction specific umbrella service agreement rather than requiring a new service agreement for each short-term firm transaction. In contrast, service agreements for firm point-to-point transmission transactions of one year or more (long-term firm transactions) are transaction specific and require a separate service agreement for each transaction.

Section 17.1

Rehearing Requests
CCEM states that the 60 days in advance to request service should be shortened to 6 days. For service shorter than one year, it argues that the procedures should not be left to negotiation with a monopolist. For service greater than one month but less than one year, it asserts that a request should be submitted 3 days in advance; for weekly service, schedules should be submitted by some specific hour the day before service is to commence; and for hourly or daily service, schedules should be submitted no later than 20 minutes in advance.

Commission Conclusion

CCEM has provided no support for its proposal to shorten the lead time for requests for firm service from sixty days to six days. Sixty days in advance of the commencement of long-term (greater than one year) firm service is not an unreasonable time period. It provides transmission providers time to conduct security analyses, as well as perform system impact studies and facility studies that may be necessary. Accordingly, CCEM's request is denied.

Section 17.2

Rehearing Requests

CCEM argues that information concerning the location of the generating facility and the load ultimately served is not required in connection with a good faith request under the Policy Statement Regarding Good Faith Request for Transmission Services and should not be required in a Completed Application. However, if it is required, CCEM argues that it should remain confidential and not be disclosed. It further asks the Commission to clarify that a point-to-point customer can designate all receipt and delivery points in order to obtain umbrella-type service and can schedule receipt and delivery points as primary or secondary and can change primary points by filing another schedule.

Commission Conclusion

We will deny CCEM's proposed changes in part as unnecessary. The locations of generating facilities and loads are needed by the transmission provider to allow it to analyze whether the requested transmission service can be accommodated over the existing transmission system, as well as to plan upgrades and transmission facility additions.[FN424]

Tariff section 17.2 already requires that "the transmission provider shall treat this [confidential] information consistent with the standards of conduct contained in Part 37 of the Commission's regulations."

With respect to CCEM's request to permit umbrella-type service, we note that we have adopted an umbrella-type service agreement approach for short-term firm transmission service, as ***12359** discussed in Section IV.G.6 (Umbrella Service Agreements).

Section 17.3

Rehearing Requests

CCEM asserts that a customer determined to be creditworthy should not have to submit a deposit for firm point-to-point transmission service. CCEM would limit this section to those customers found not to be creditworthy and asks the Commission to clarify that only the costs of system impact studies or facilities studies can be deducted from the deposit.

Commission Conclusion

Section 17.3 reflects a standard requirement in many existing tariffs and other agreements on file with this Commission. CCEM provides no compelling reason to revise this tariff provision.

We also deny CCEM's request regarding deductions from the deposit. We will not preclude a utility from demonstrating that it incurs costs other than system impact studies or facilities studies in processing a service application and arguing that these costs should be deducted from a deposit.

Section 17.4

Rehearing Requests

CCEM argues that a deficiency determination should be made in, at most, one day.

Commission Conclusion
CCEM provides no compelling reason to revise this tariff provision. CCEM's argument also ignores the fact that certain applications involve more complex unique transactions and associated arrangements which may require more time to review than other more standard applications. CCEM's apparent concern regarding deficient applications should be mitigated by the pro forma tariff requirement that the transmission provider must attempt to remedy minor deficiencies in the application informally with the transmission customer.

Section 17.5

Rehearing Requests
CCEM asserts that a transmission provider should respond to a completed application for firm transmission service within 10 minutes for hourly service, 10 minutes for daily service, 4 hours for weekly service, 1 day for monthly service, 2 days for service longer than one month but less than one year, and 5 days for service one year or longer.

Commission Conclusion
Section 17.5 requires the transmission provider to notify the eligible customer as soon as practicable, but no later than 30 days after receipt of a completed application if it can provide the service or if a system impact study will be required. We do not believe that further specificity in establishing deadlines for each type of service and duration of service is necessary. However, we are clarifying section 17.5 to require that all responses be made on a non-discriminatory basis. If CCEM believes the transmission provider is engaging in discriminatory behavior by delaying responses to service requests (or by responding to service requests by its wholesale merchant function more quickly than it responds to service requests by unaffiliated customers), it can file a section 206 complaint with the Commission.

Section 17.7

Rehearing Requests
Several utilities ask the Commission to clarify that, if transmission facilities have been constructed to accommodate a request for transmission service, delays by the customer in commencing service should be prohibited or the customer should pay the full carrying charges on the facilities during the period of delay (less any revenues received).[FN425] Similarly, EEI and Southern argue that if new facilities are constructed, but the customer postpones service by paying a reservation fee, fairness requires that the customer bear its cost responsibility for the new construction at the time the facilities are ready to be used.

Commission Conclusion
Because different factual circumstances could exist that may lead to alternative solutions to the problem, we will not adopt a generic resolution. Rather, the Commission believes it appropriate to allow each utility to propose solutions in subsequent section 205 filings with the Commission.

Section 19

Rehearing Requests
VA Com asks the Commission to clarify that determining the necessity of a transmission facility upgrade or addition remains a state prerogative. It asserts that native load customers may face reduced reliability, or may incur costs associated with premature additions, if calculations of ATC are incorrect. In addition, it asserts that generating facilities can also be used to relieve regional capacity constraints—"For example, a current proposal by Virginia Electric and Power Company ("Virginia Power") seeks the Virginia Commission's approval of a major new transmission line. Virginia Power alleges that the line is needed since it would

increase the availability of emergency off-system supplies and allow it to lower its capacity reserve requirements. If the Virginia Commission were to approve the line, it is conceivable that FERC could direct Virginia Power to use this additional interchange capability to facilitate wholesale wheeling transactions. In such an event, native load customers may be adversely affected since the utility would be forced to suffer diminished reliability or build additional generation or transmission facilities." (VA Com at 10-12). CCEM asks the Commission to require studies for short-term firm point-to-point service or requests for capacity that are posted on the OASIS.

Commission Conclusion

In the Final Rule, the Commission explicitly stated that public utilities may reserve existing transmission capacity needed for native load growth and network transmission customer load growth reasonably forecasted within the utility's current planning horizon. However, any capacity that a public utility reserves for future growth, but is not currently needed, must be posted on the OASIS and made available to others through the capacity reassignment requirements, until such time as it is actually needed and used.[FN426]

This ability to reserve capacity to meet the reliability needs of native load would apply equally to transmission built in the future. VA Com requested clarification of the intended treatment by the Commission in the ATC calculation of a transmission line built in lieu of generation for purposes of lowering reserve requirements for native load. If it seeks to withhold capacity in response to a request for service by an eligible customer, the transmission provider will have the burden of proof to demonstrate that any reserved capacity is needed for meeting native load and network customers' load growth or for purposes of meeting a reserve requirement level that is reasonable.

CCEM's request is unnecessary because system impact studies and facilities studies are required pursuant to tariff section 19 for both long-term and short-term firm point-to-point transmission service. ***12360**

Sections 19.2 and 32.2

Rehearing Requests

Utilities For Improved Transition and VEPCO ask the Commission to modify these sections to require that a system impact study agreement specify the estimated charge instead of the maximum charge so that the transmission provider may collect all prudently incurred study costs.

Commission Conclusion

Utilities For Improved Transition and VEPCO correctly note that the use of the phrase "maximum" in the language of tariff sections 19.2 and 32.2 may prevent a utility from collecting the full costs of conducting a system impact study despite acting in a prudent manner. Accordingly, the relevant portion of these sections are modified as shown below to eliminate this potential inequity (deleted text in brackets):

(i) The System Impact Study Agreement will clearly specify [the maximum charge, based on] the Transmission Provider's estimate of the actual cost, and time for completion of the System Impact Study. The charge shall not exceed the actual cost of the study.

Sections 19.3 and 19.4

Rehearing Requests

TAPS asserts that the 15-day periods for customers to execute a service agreement after completion of a system impact study are too short and should be lengthened to 30 days or the transmission provider should be allowed to provide an extension for cause (with public notice) while the customer is pursuing an agreement in good faith.

Commission Conclusion

TAPS' proposed changes are not necessary because the eligible customer is provided a sufficient response time considering the situation to which the eligible customer is responding. Specifically, the 15-day period in section 19.3 refers to the situation where the transmission provider has conducted a system impact study and concluded that the requested service can be provided without the need to modify its transmission system. TAPS provides no reason why the eligible customer requesting the service should not be prepared to immediately accept the offer to provide service at the transmission provider's standard rate (without the need for upgrades, the eligible customer would not be assessed incremental transmission charges).

Similarly, the 15-day period in section 19.4 refers to the time in which the eligible customer has to execute a facilities study agreement in which it agrees to pay the transmission provider for the costs of conducting a facilities study. In contrast, when the facilities study is completed and the eligible customer is provided with a good faith estimate of any direct assignment facilities and/or share of any network upgrades, section 19.4 provides the eligible customer with 30 days to respond.

Section 22.1(d)

Rehearing Requests

Utilities For Improved Transition and Florida Power Corp ask the Commission to modify this section to require that a request for modification of service on a non-firm basis be made by submitting a modification to the original application with an OASIS posting. Otherwise, they assert, this section implies that such modifications would occur without using the transmission provider's OASIS.

Commission Conclusion

Utilities For Improved Transition and Florida Power Corp misinterpret this section of the tariff. The Commission's intention is simply to clarify that the customer's request to modify its firm transmission service to receive service over secondary receipt and delivery points on a non-firm basis would not require a separate application for non-firm transmission service. The concerns expressed with respect to posting on the OASIS are addressed in Order No. 889-A.

Section 23.1

Rehearing Requests

CCEM asserts that the Commission sHhould specify the filings necessary for assignment of service referenced in this section or delete the clause. In addition, CCEM asks the Commission to clarify that the identical services will be provided at no additional cost to the assignee or the reseller.

Commission Conclusion

The pro forma tariff is a tariff of general applicability. For administrative reasons, the listing of every conceivable situation in which an assignment or transfer of service from one entity to another may require a separate filing is not feasible. For example, if the Commission lists only a single situation that requires a separate filing and subsequently determines another situation would also require a filing, all of the pro forma tariffs on file with the Commission would need to be revised to reflect the change.

CCEM's request that the Commission clarify that reassigned services will be provided at no extra cost is also denied. CCEM ignores the fact that nothing in the pro forma tariff prevents the transmission provider from seeking a change in rates pursuant to a section 205 filing whether such filing relates to a general increase in rates to all transmission customers or to additional costs the transmission provider asserts it incurs due to providing service to an assignee. As always, the transmission provider bears the burden of proof of demonstrating that its proposal is just and reasonable.

Section 23.2

Rehearing Requests
CCEM asks the Commission whether an assignee can change primary points if there is only a partial assignment.

Commission Conclusion
Whether the assignment is full or partial is immaterial. If an assignee wishes to change its receipt or delivery points on a firm basis (full or partial), the request will be treated as a new request for service as required under tariff sections 22.1 and 23.1. However, if an assignee wishes to change receipt or delivery points on a non-firm (full or partial) basis, such change can be accomplished without the need for a new service agreement as provided in pro forma tariff section 22.1.

Sections 25 and 34

Rehearing Requests
VT DPS asks the Commission to revise these sections to state that "all firm customers should share in non-firm revenues" consistent with the language of the preamble.

Commission Conclusion
VT DPS' request is denied. The Commission did not intend to mandate the rate methodology used to reflect any cost reductions that may be associated with the provision of non-firm transmission service. While the Commission would generally expect all firm customers to share in non-firm revenues, the use of revenue credits is not the only acceptable method of reflecting non-firm system usage. The transmission provider's method of reflecting revenues from non-firm service should be addressed on a case-by-case basis.

Section 29.1

Rehearing Requests
TAPS contends that, to avoid improper use of operating agreements by transmission providers, the ***12361** Commission should either permit network operating agreements to be filed in unexecuted form or include a network operating agreement as part of the pro forma tariff.

Commission Conclusion
The network operating agreement is expected to be a highly detailed agreement between the transmission provider and network customer that establishes the integration of the network customer within the transmission provider's transmission system. Due to the unique characteristics of network customers' systems and the level of customer-specific information and arrangements required under a network operating agreement, it is likely that each network operating agreement will be different for each customer. Accordingly, the Commission does not believe it appropriate to mandate a particular form of network operating agreement for inclusion in the pro forma tariff. However, if a transmission provider wishes to include a generic form of network operating agreement in its pro forma tariff (to be modified as required and as mutually agreed to on a customer-specific basis), it may propose to do so in a section 205 filing or it may file an unexecuted network operating agreement in a section 205 filing.

To the extent a customer believes a transmission provider is engaging in unduly discriminatory practices via the network operating agreement, the customer may file a section 206 complaint with the Commission.

Section 29.4

Rehearing Requests
TDU Systems asserts that this section does not identify who should determine what facilities are "necessary to reliably deliver capacity and energy. * * *" It asks the Commission to clarify that this is solely the responsibility of the transmission customer.

Commission Conclusion
TDU Systems' argument ignores tariff section 35.1, which specifies:

[t]he Network Customer shall plan, construct, operate and maintain its facilities in accordance with Good Utility Practice and in conformance with the Network Operating Agreement. (emphasis added)

Accordingly, the determination of what network customer facilities are "necessary to reliably deliver capacity and energy * * *" is to be agreed upon by both the transmission provider and network customer and specified in the network operating agreement. To the extent the parties do not agree, the transmission provider will file an unexecuted network operating agreement with the Commission and we will resolve the dispute.

Section 30.1

Rehearing Requests
VT DPS argues that, consistent with section 30.7, section 30.1 should not require that a network resource be available on a strictly non-interruptible basis.

Commission Conclusion
VT DPS' request is denied. The Commission believes that a network customer should only be allowed to designate non-interruptible network resources. To allow otherwise would interfere with the planning process as well as the day-to-day operation of the transmission system to integrate resources with customer's loads (e.g., the transmission provider will be unable to plan for what generation resource will be available to meet a customer's load in the event its designated resource is subject to interruption). Similarly, for operational purposes on a day-to-day basis, an interruption of a network customer's designated resource could cause a transmission constraint.[FN427] Because constraints affecting reliability may lead to curtailment or redispatch of all network resources, other network customers would be affected by such interruptions on a load-ratio basis. However, to the extent a network customer wishes to use an interruptible generation source, it can still use this generation source on an as-available basis to import energy to serve its load pursuant to pro forma tariff section 28.4.

Section 30.4

Rehearing Requests
PA Coops ask the Commission to modify this section "to permit the Network Resources to be operated at outputs that exceed the Network Customer's designated Network Load plus losses when the Network Resource's output is being sold to a third party or the Network Resource is called upon to be operated by the Network Customer's power pool, ISO or control area operator." (PA Coops at 8-9). Similarly, Santa Clara and Redding ask the Commission to modify the last sentence to state: "* * * exceeds its designated Network Load, plus non-firm sales delivered under Part II, plus losses" so that network resources will not remain idle when they could otherwise generate non-firm power and energy for sale at competitive prices.

In addition, TDU Systems argues that the arbitrary limits on the ability of network customers to operate Network Resources prevents economic dispatch or the use of resources to meet load requirements and limits the ability to schedule the output of Network Resources between and among control areas, effectively preventing the network customer from operating an integrated system.[FN428] TDU Systems asserts that the Commission should not presume that a network customer's economic dispatch will burden a transmission provider, but should require a transmission provider to demonstrate that such a burden will occur. TAPS asks the Commission to clarify this section so as to bar not the operation of network resources in excess of network load, but rather the usage of network service in connection with operation of such resources in excess of network load. TAPS adds that section 30.4 is contrary to FMPA v. FPL, 74 FERC at 61,014-15. AEC & SMEPA argues that the Commission should provide the necessary latitude for such resources to be used across multiple control areas to service the total load of transmission users.

Commission Conclusion

Preliminarily, TDU Systems and others' argument that a designated network resource must consist of the entirety of a generating unit is mistaken, as we explained in sections 1.22 and 1.25 above. The Commission's intent in requiring that the output of network resources not exceed network load plus losses is to prevent designated network resources from being used to make firm sales to third parties. This is consistent with the pro forma tariff's requirement in sections 1.25 and 30.1 that:

Network Resources may not include resources, or any portion thereof, that are committed for sale to non-designated third party load or otherwise cannot be called upon to meet the Network Customer's Network Load on a non-interruptible basis.

Absent a requirement that network resources always be available to meet a customer's network loads, reliability of service to the network customer as well as to native load and other network customers could be affected, as we describe in detail in section 30.1 above. If a network customer desires to enter into a firm sale from its designated network resources or use such network resources for meeting reserve requirements, it must eliminate the appropriate resources or portions thereof from its designated network ***12362** resources pursuant to pro forma tariff section 30.

Santa Clara, Redding and others contend that this limitation improperly restricts the use of network resources for non-firm sales. It was not the Commission's intent to prohibit the network customer from engaging in non-firm sales from idle designated network resources. We find that the non-firm operation of network resources will not affect the availability of such resources on a firm basis because such non-firm uses are subject to interruption. Accordingly, the Commission's concerns regarding the reliable provision of network service are satisfied.

Furthermore, as noted by Pennsylvania Coops, emergencies could arise in which the transmission provider may request that a network customer alter the operation of its network resources in response to a contingency, which action could result in a violation of the limitation in section 30.4. Therefore, the Commission believes an exception to the network resources output limitation is also appropriate for such emergency situations. Accordingly, tariff section 30.4 is revised, in relevant part, consistent with the above findings, as shown below (emphasis added):

The Network Customer shall not operate its designated Network Resources located in the Network Customer's or Transmission Provider's Control Area such that the output of those facilities exceeds its designated Network Load, plus non-firm sales delivered pursuant to Part II of the Tariff, plus losses. This limitation shall not apply to changes in the operation of a Transmission Customer's Network Resources at the request of the Transmission Provider to respond to an emergency or other unforeseen condition which may impair or degrade the reliability of its Transmission System.

The remaining concerns expressed by TDU Systems with respect to the economical operation of a network customer's loads and resources located in multiple control areas are addressed above in Section IV.G.1.b. (Network and Point-to-Point Customers' Uses of the System (so-called "Headroom")).

Section 30.6

Rehearing Requests
CSW Operating Companies asks the Commission to clarify that a customer has the obligation to replace the loss of a resource that is not physically interconnected with the transmission provider's transmission system within the time that is customary in the region or be subject to curtailment and suggests language to be included as section 33.8. CSW Operating Companies indicates that it intends to include a provision addressing this issue in the form of a network operating agreement included in the individual companies' Final Rule compliance tariffs.

Commission Conclusion
The Commission agrees with CSW Operating Companies that the appropriate place to address detailed operational requirements such as this is the Network Operating Agreement. If disputes arise, they can be addressed on a case-by-case basis.

Section 30.7

Rehearing Requests
Wisconsin Municipals asks the Commission to clarify that, for purposes of comparability between network and point-to-point customers, a customer may not reserve capacity for firm point-to-point transmission service until the customer can show that it owns or has committed to purchase generation under an executed contract that it intends to use over the reserved transmission contract path. Wisconsin Municipals claims that without the requirement to demonstrate ownership or contractual rights to the output of a generation resource, the point-to-point customers will have the advantage over network customers of being able to reserve transmission service over facilities with limited available transmission capacity earlier than network customers. Wisconsin Municipals also argues, in essence, that a single or a few point-to-point customers would be able to engage in hoarding of transmission capacity by reserving all available transmission capacity over certain transmission facilities.

Commission Conclusion
The arguments presented by Wisconsin Municipals in support of its proposal are misplaced. Wisconsin Municipals' assertion that point-to-point customers would be able to reserve transmission service over facilities with limited available transmission capacity earlier than network customers overlooks the fact that the Final Rule allows transmission providers to reserve existing transmission capacity needed for native load growth and network transmission customer load growth reasonably forecasted within the transmission provider's current planning horizon.[FN429] Wisconsin Municipals' concerns regarding hoarding of transmission capacity are answered in Section IV.C.6. (Capacity Reassignment). Finally, Wisconsin Municipals' argument that comparability requires that both network and point-to-point customers be required to demonstrate ownership or contractual rights to the output of a generation resource is not persuasive. Network and firm point-to-point transmission service are different services. Firm point-to-point transmission service is available for periods as short as one day, whereas network service is designed to accommodate a longer term of service with a minimum term of service of one year. The requirement to demonstrate ownership or contractual rights to generation for network service is necessary because the transmission provider must be able to serve the network load from any of the designated resources. In contrast, point-to-point service is a capacity reservation service between specified points of receipt and points of delivery. Accordingly, this network requirement does not need to be extended to firm point-to-point service under the guise of comparability.

Section 31.2

Rehearing Requests
TDU Systems asks the Commission to clarify that an application for new network load for an existing network customer need only address the additional network service needed to serve the new Network Load and does not in any way implicate the existing network service for which the network customer has already contracted.

Commission Conclusion
No clarification is necessary. Tariff section 31.2 explicitly states in relevant part:

A designation of new Network Load must be made through a modification of service pursuant to a new Application. (Emphasis added)

Section 32.3

Rehearing Requests
TDU Systems asserts that this section requires too short a time for customers to evaluate a system impact study. It argues that, at a minimum, customers should have 60 days to evaluate a study and, in the event of a dispute, the application should remain viable until the dispute is resolved (also argues that the time periods set forth in sections 19.1, 19.4, 32.1, 32.3 and 32.4 are too short).

Commission Conclusion
TDU Systems' proposed changes are not necessary as the pro forma tariff provides an eligible customer sufficient time to respond to a system impact ***12363** study. Specifically, the 15-day period in section 32.3 refers to a situation where the transmission provider has conducted a system impact study and concluded that the requested service can be provided without the need to modify its transmission system. TDU Systems provides no reason why the eligible customer should not be prepared to immediately accept the offer of providing service at the transmission provider's standard rate (without the need for upgrades, the eligible customer would not be assessed incremental transmission charges).

Similarly, the 15 day period in sections 19.1, 19.4, 32.1 and 32.4 refer to the time in which the eligible customer has to agree to execute an agreement to pay the transmission provider for costs of conducting studies (a system impact study in sections 19.1 and 32.1 and a facilities study in sections 19.4 and 32.4). TDU Systems provides no reason why it should not be prepared to accept or reject the relatively minor costs of further studies to determine whether its requested transmission service can be accommodated by the transmission provider.

In contrast, when the facilities study is completed and the eligible customer is provided with a good faith estimate of any direct assignment facilities and/or share of any network upgrades, the eligible customer is given 30 days to respond, which is more than a sufficient time.

Sections 33.2 and 34.4

Rehearing Requests
TAPS asserts that the Commission cannot shunt aside the need for ongoing revenue crediting to reduce transmission charges as a rate issue, while allowing monthly redispatch costs to be collected monthly in charges under the tariff. It contends that the Commission must require revenues to be shared on an ongoing, load-ratio basis.

Commission Conclusion
As discussed above, redispatch of all Network Resources and the transmission provider's own resources is only to be performed to maintain the reliability of the transmission system, not for economic reasons. As a result, the frequency of redispatch charges being assessed to network customers is expected to be infrequent. In addition, the Commission is according substantial flexibility to public utilities to propose appropriate pricing terms in their compliance tariff, which includes the treatment of revenue credits. As mentioned above, there are several methods that utilities can use to properly reflect a benefit from non-firm transmission service to firm transmission customers. We do not believe it appropriate to mandate a specific method, such as automatic

monthly flow through of revenue credits, at this time. However, TAPS may pursue this issue when utilities file their compliance rates or subsequent 205 rate filings.

Section 34.3

Rehearing Requests

Several utilities assert that because the monthly transmission system load is composed in part of the contract demands of all firm point-to-point transmission customers and under the Rule the charge for firm point-to-point service may be derived by dividing the transmission cost of service by the sum of the transmission provider's 12 monthly peak firm transmission loads, the transmission provider is prevented from recovering its entire cost of service.[FN430]

Maine Public Service states that parties should be allowed to argue on a case-by-case basis that firm transmission revenues should be credited instead of including the demands in the denominator (it indicates that this issue is pending in Docket No. ER95-836). It asserts that the revenue credit method would prevent transmission providers that offered discounts from unjustly being penalized for that decision and is the only method that permits utilities to have an opportunity to recover their costs. It adds that the Commission established procedures to keep gas pipelines whole in this same situation.

Commission Conclusion

While the Commission established one method of calculating load ratios and allocating costs in Order No. 888,[FN431] utilities are free to propose alternative pricing methodologies in a section 205 filing consistent with the Commission's Transmission Pricing Policy Statement.[FN432] We note, however, such utilities will have the burden of demonstrating that these methods would not result in over-collections of their revenue requirement.

Section 34.4

Rehearing Requests

TDU Systems asks the Commission to clarify, as a matter of comparability, that any mechanism proposed by a transmission provider to collect charges based on opportunity costs associated with redispatch must provide for the collection of other customers' like costs and payments to those customers.

Commission Conclusion

This issue is addressed in Section IV.G.1.e. (Opportunity Cost Pricing).

Schedules 7 and 8

Rehearing Requests

TAPS asks the Commission to clarify that these schedules do not approve “heightened” charges for short-term services.

Commission Conclusion

The Commission did not specify transmission rates for any tariff services in Order No. 888. The rates for long-term firm transmission, short-term firm transmission and non-firm transmission services are to be proposed by the transmission provider, as listed on Tariff schedules 7 and 8, and filed with the Commission. TAPS' argument regarding “heightened” charges for these services is therefore premature. TAPS is free to raise this concern at such time as utilities file their proposed transmission rates.

Attachment G

Rehearing Requests
Santa Clara and Redding ask the Commission to modify Attachment G so that, where interconnection/operational standards are in place and working effectively, additional standards are not imposed simply as a result of switching to the pro forma tariff from its current interconnection service.

Commission Conclusion
The pro forma tariff does not specifically require that the network operating agreement between the transmission provider and network customer must be a new agreement. However, the network operating agreement is expected to be a highly detailed agreement between the transmission provider and network customer establishing the integration of the network customer within the transmission provider's transmission system. Existing agreements between the customer and transmission provider may not provide all of the information required or make all of the technical arrangements required under the pro ***12364** forma tariff (e.g., redispatch and ancillary services information and arrangements.) Nevertheless, to the extent the transmission customer is currently receiving network integration transmission service or similar service and its present interconnection agreement fully comports with the requirements of the terms and conditions of the tariff including the informational requirements specified in tariff sections 33 and 35, then the present interconnection/operations agreement can be substituted for a network operating agreement or modified appropriately.

9. Miscellaneous Tariff Administrative Changes
Due to administrative oversight, certain tariff sections require minor corrections or modifications. Because of the administrative nature of these changes, we believe that no further discussion is needed.

Section 12.1 Internal Dispute Resolution Procedures

—Changes “Transmission Service” to “transmission service”

Section 13.6 Curtailment of Firm Transmission Service

—Changes the description regarding curtailment of multiple transactions to:

the Transmission Provider will curtail service to Network Customers and Transmission Customers taking Firm Point-To-Point Transmission Service on a basis comparable to the curtailment of service to the Transmission Provider's Native Load Customers.

10. Pro Forma Tariff Compliance Filings
Absent a waiver, all public utilities must submit, no later than July 14, 1997, a compliance filing that reflects the tariff changes set forth in this order on rehearing.[FN433]

A conforming pro forma tariff, containing all the revisions and clarifications contained in this order on rehearing, is attached as Appendix B. In addition, an electronic version of the conforming pro forma tariff will be made available on the Commission's electronic bulletin board service (Commission Issuance Posting System (CIPS)) in redline/strikeout form in WordPerfect 5.1 format.

H. Implementation
In the Final Rule, the Commission set forth the details of the implementation procedures and included special implementation requirements for coordination arrangements (power pools, public utility holding companies, and bilateral coordination arrangements).[FN434]

The Revised Procedures

The Commission adopted slightly different implementation procedures for Group 1 public utilities (tendered for filing open access tariffs before the date of issuance of the Rule) and for Group 2 public utilities (did not tender for filing open access tariffs before the date of issuance of the Rule).

1. Group 1 Public Utilities

In the Final Rule, the Commission required Group 1 public utilities, within 60 days following publication of the Final Rule in the Federal Register, to make section 206 compliance filings that contain the non-rate terms and conditions set forth in the Final Rule pro forma tariff and identify any terms and conditions that reflect regional practices, as discussed below.[FN435]

As to rates, the Commission noted that a transmission tariff rate is already in effect for all Group 1 public utilities, except for the few with recently-tendered applications that have not yet been accepted for filing.

The Commission noted, however, that if a Group 1 public utility determined that certain rate changes are necessitated by the revised non-rate terms and conditions, it may file a new rate proposal under FPA section 205. The Commission indicated that such filings must be "conforming"[FN436] under the Transmission Pricing Policy Statement and must be made no later than 60 days after publication of the Final Rule in the Federal Register and intervenors may raise any concerns with the filings within 15 days after such filings.[FN437] The Commission imposed a blanket suspension for any filings by Group 1 public utilities proposing rate changes necessitated by the new non-rate terms and conditions. The Commission further indicated that these rates will go into effect, subject to refund, 60 days after publication of this Rule in the Federal Register (the same day on which the non-rate terms and conditions of the Final Rule pro forma tariff go into effect).

2. Group 2 Public Utilities

In the Final Rule, the Commission indicated that Group 2 public utilities will be treated the same as Group 1 public utilities with regard to non-rate terms and conditions, but will be treated slightly differently from Group 1 as to rates, since Group 2 utilities have not filed any proposed rates.[FN438] The Commission required these utilities to either: (i) within 60 days following publication of the Final Rule in the Federal Register, make section 206 compliance filings that contain the non-rate terms and conditions set forth in the Final Rule pro forma tariff and identify any terms and conditions that reflect regional practices, as discussed below; and (ii) within 60 days following publication of the Final Rule in the Federal Register, make section 205 filings to propose rates for the services provided for in the tariff, including ancillary services; or (iii) make a "good faith" request for waiver. The Commission added that the rates must meet the standards for conforming proposals in the Commission's Transmission Pricing Policy Statement and comply with the guidance concerning ancillary services set forth in this order.

The Commission explained that intervenors may raise any concerns with these filings within 15 days after the filing.[FN439] The Commission imposed a blanket suspension for all such rate filings and indicated that they will go into effect, subject to refund, 60 days after the publication of this Rule in the Federal Register (the same day on which the terms and conditions of the compliance tariffs go into effect).

3. Clarification Regarding Terms and Conditions Reflecting Regional Practices

In the Final Rule, the Commission explained that it had built a degree of flexibility into the tariffs to accommodate regional and other differences. [FN440] It explained that certain non-rate Final Rule pro forma tariff provisions specifically allow utilities either to follow the terms of the provision or to use alternatives that are reasonable, generally accepted in the region, and consistently adhered to by the transmission provider (e.g., time deadlines for scheduling changes, time deadlines for determining available capacity). In addition, it explained that other tariff provisions require utilities to follow Good Utility Practice (section 1.14 of the Final Rule pro forma tariff).

4. Future Filings
In the Final Rule, the Commission indicated that once the compliance tariff and conforming rates go into effect, which would be 60 days after publication of the Rule in the Federal Register, a public utility (either Group 1 or Group 2) may file pursuant to section 205 a tariff with terms and conditions that differ from those set forth in this Rule, provided that, among other things, it demonstrates that such terms and conditions are consistent with, or superior to, those in the compliance tariff.[FN441] However, the Commission emphasized that the public utility may not seek to litigate fundamental terms and conditions set forth in the Final Rule. In addition, the Commission explained that the public utility may file whatever rates it believes are appropriate, consistent with the Transmission Pricing Policy Statement.

5. Waiver
In the Final Rule, the Commission found that it is reasonable to permit certain public utilities for good cause shown to file, within 60 days after the Rule is published in the Federal Register, requests for waiver from some or all of the requirements of this Rule.[FN442] The Commission explained that the filing of a request in good faith for a waiver from the requirement to file an open access tariff will eliminate the requirement that such public utility make a compliance filing unless thereafter ordered by the Commission to do so. The Commission emphasized, however, that it will not exempt such public utility from providing, upon request, transmission services consistent with the requirements of the Final Rule.

Rehearing Requests
Wisconsin Municipals asserts that the Commission should "require utilities (if requested by their customers) to honor the settlements to which they have agreed and to file the pro forma tariff, modified to incorporate settlement provisions that exceed the minimum provisions of the pro forma tariff, as their implementational filing." Alternatively, it asks that the Commission "require parties with settlements to make a Section 205 filing one day following their implementation filing, change any rates, terms and conditions in the pro forma tariff as necessary to incorporate any superior provisions from their settlement tariffs into the pro forma tariff, and seek any waivers necessary to make the settlement tariff effective immediately." (Wisconsin Municipals at 7-10).

Blue Ridge requests rehearing of the "unbalanced tariff implementation process that rolls over the due process rights of transmission customers." It asserts that utilities should not have the right to file a "'Good Utility Practices,' blank check variance for regional practices in the compliance docket." (Blue Ridge at 33-35). Blue Ridge further requests that Group 1 utilities file compliance tariffs in the same docket as their pending open access dockets and asks that subsequent changes be in a separate docket as a new general rate case. Blue Ridge also states that the Commission should explicitly mention that customers have the right to file section 206 requests to change the tariffs.

Indianapolis P&L argues that the pricing requirements are unjust, unreasonable, unlawful, confiscatory and an abuse of discretion as to Indianapolis P&L. It asserts that its rates are not based on embedded, original cost, but, as a matter of Indiana law, its utility property is valued at the "fair value," which exceeds the embedded original cost of such property. It declares that it is impossible for Indianapolis P&L to comply with both the comparability requirement and the requirement that transmission rates be based on original cost. It states that the requirement to provide transmission service and generation-based ancillary services at rates based on original cost is not comparable to Indianapolis P&L's own use of its assets. Accordingly, it argues that the Commission should allow Indianapolis P&L to set its initial open access rates on a fair value, long-run marginal cost basis. Alternatively, it states that the Commission could grant Indianapolis P&L a waiver from the requirements of the Open Access Rule.

Indianapolis P&L further argues that the imposition of an obligation to enlarge generation to provide ancillary services is beyond the Commission's statutory authority. It explains that Indianapolis P&L is an incidental transmission owner and a relatively small public utility and asks that the Commission grant it waiver from the requirements of open access and OASIS. In deciding whether to grant a waiver, it asserts that the Commission should also consider system size and configuration, the amount of wholesale revenues or MWH sales, or the availability of competing transmission paths.

Union Electric argues that the final rules violate procedural due process and that the implementation schedule is unrealistically ambitious. It argues that where the final rules call for changes from the NOPRs that could not be reasonably anticipated, they amount to deprivation of due process and rights to fairness in the administrative process. Indeed, it points out, the Commission itself has not even completed its promulgation of the OASIS Final Rule Union Electric is concerned that it has not had an adequate time to comply with and comment on the rules.

Commission Conclusion

Wisconsin Municipals has misinterpreted the Commission's findings in Order No. 888, and thus its concerns are without merit. While it is true that Order No. 888 requires all public utilities to make compliance filings containing the non-price terms and conditions set forth in the Final Rule pro forma tariff,[FN443] Order No. 888 also states that "we are not abrogating existing requirements and transmission contracts generically. * * *" [FN444] In short, the Commission is not requiring (or even generically allowing) the abrogation of existing transmission contracts, but is only requiring that jurisdictional transmission providers must also offer transmission service under the Final Rule pro forma tariff in addition to whatever commitments the provider will continue to have under its existing contracts. [FN445]

As to Wisconsin Municipals' assertions that prior individual settlement provisions may exceed the ***12366** minimum provisions of the pro forma tariff, the Commission believes that such arguments should be addressed on a case-by-case basis. [FN446]

Two additional points are pertinent. First, we note that although we are not generically abrogating existing transmission contracts, utilities retain whatever existing rights they had to propose unilateral changes under section 205 of the FPA if they want to convert a customer to service under the tariff, and customers retain their section 206 right to seek reformation of existing transmission contracts if they are unjust, unreasonable, unduly discriminatory or preferential. Second, where a utility has treated similarly-situated customers differently—serving one under a more favorable bilateral contract and another under a less favorable tariff provision—traditional undue discrimination remedies may be available.

We deny Blue Ridge's rehearing requests because the Commission does not intend to assume the regulatory responsibility of identifying in the first instance all of the regional practices around the country that could (and should) properly be reflected in the compliance tariffs. Transmission customers opposed to deviations related to regional practices not only had the opportunity to protest the compliance filings when they were tendered, [FN447] but these customers also have the right to file section 206 requests to change these tariffs at any time. In addition, Blue Ridge's request that customers be given 45 days to respond to compliance filings instead of 15 days is moot. In an order issued July 2, 1996,[FN448] we took three actions to address this concern: (1) we gave entities 30 days, instead of 15 days, to respond to Order No. 888 compliance filings; (2) we agreed to post an electronic version of all Order No. 888 compliance filings on the Commission's Electronic Bulletin Board; and (3) we required all public utilities making a compliance filing to also serve a copy of their filing on electronic diskette to any eligible customer or state regulatory agency requesting a copy. We believe that these actions not only provided all interested parties with access to the compliance filings more quickly, but also provided these parties sufficient time to analyze the information once they received it.[FN449] Moreover, the time periods provided for making and responding to Order No. 888 compliance filings have expired.

With regard to Blue Ridge's first clarification request, we provide the following guidance. Utilities that had pending open access filings at the time that the Final Rule was implemented had the non-price terms and conditions of those pending tariffs superseded by their Order No. 888 compliance filings. Any customer concerns about the non-rate tariff terms and conditions in the compliance filing should be raised in the compliance docket, and any future customer concerns should be raised in a separate, future section 206 complaint filed by the customer.

Furthermore, we reject Indianapolis P&L's rate issue because, if this utility believes that it operates under special circumstances that require it to use "non-conforming" pricing methods, it is free to file such a proposal under section 205. The merits of Indianapolis P&L's arguments are more appropriately addressed in such a section 205 proceeding. The Commission will not alter its generic policy (which is the subject of this rulemaking) merely to address the particular needs of one party.

In addition, with regard to both of Indianapolis P&L's concerns, we note that pursuant to the Commission's July 2 Order, the Commission indicated that it would not address waiver requests in a generic proceeding and that parties would have to file such requests separately for separate docketing. We further note that Indianapolis P&L filed a separate waiver request on July 9, 1996, which was docketed as OA96-81.[FN450]

We also reject Union Electric's argument that the final rules violate procedural due process. Union Electric has had every opportunity to raise arguments with regard to every step in the Commission's derivation and implementation of the final rules. Moreover, with regard to Union Electric's claim that it was given an inadequate amount of time to comprehend and implement the final rules, we note that virtually every public utility, including Union Electric, complied with the Open Access Rule on a timely basis, and there have been very few complaints that the rules are hard to comprehend.

I. Federal and State Jurisdiction: Transmission/Local Distribution

In the Final Rule, the Commission explained that after reviewing the extensive analysis of the FPA, legislative history, and case law contained in both the initial Stranded Cost NOPR and in the Open Access NOPR, and the comments received on that analysis, it reaffirmed its assertion of jurisdiction over the transmission component of an unbundled interstate retail wheeling transaction.[FN451] The Commission also reaffirmed and clarified its determinations regarding the tests to be used to determine what constitute Commission-jurisdictional transmission facilities and what constitute state-jurisdictional local distribution facilities in situations involving unbundled wholesale wheeling and unbundled retail wheeling.

The Commission also explained that where states unbundle retail sales, it will give deference to their determinations as to which facilities are transmission and which are local distribution, provided that the states, in making such determinations, apply the seven criteria discussed in the NOPR and reaffirmed by the Commission. In addition, the Commission clarified that there is an element of local distribution service in any unbundled retail transaction, and further clarified other aspects of its jurisdictional ruling to preserve state jurisdiction over matters that are of local concern and will remain subject to state jurisdiction if retail unbundling occurs.

The Commission reaffirmed its legal determination that if unbundled retail transmission in interstate commerce occurs voluntarily by a public utility or as a result of a state retail access program, this Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission. The Commission found compelling the fact that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.

The Commission further explained that when a retail transaction is broken into two or more products that are sold separately, the jurisdictional lines change. In this situation, the Commission emphasized that the state clearly retains jurisdiction over the sale of the power, but the unbundled ***12367** transmission service involves only the provision of "transmission in interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission.

The Commission recognized that in asserting jurisdiction over unbundled retail transmission in interstate commerce by public utilities, it was in no way asserting jurisdiction to order retail transmission directly to an ultimate consumer. It explained that its assertion of jurisdiction is that if unbundled retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

The Commission further clarified that nothing in its jurisdictional determination changes historical state franchise areas or interferes with state laws governing retail marketing areas of electric utilities. It explained that while its jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over transmission in interstate commerce by public utilities.

The Commission also adopted a new section 35.27(b) as follows:

Nothing in this part (i) shall be construed as preempting or affecting any jurisdiction a state commission or other state authority may have under applicable state and federal law, or (ii) limits the authority of a state commission in accordance with state and federal law to establish (a) competitive procedures for the acquisition of electric energy, including demand-side management, purchased at wholesale, or (b) non-discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

With respect to the Commission's adoption of the Open Access NOPR's functional/technical tests for determining what facilities are Commission-jurisdictional facilities used for transmission in interstate commerce and what facilities are state-jurisdictional local distribution facilities, the Commission concluded that it could not divine a bright line for unbundled retail transmission by the public utility that previously provided bundled retail service to the end user. The Commission added that the limited case law, including Connecticut Light & Power Company v. FPC (CL&P) and Federal Power Commission v. Southern California Edison Company (the Colton case),[FN452] supports a case-by-case determination.[FN453] Accordingly, the Commission stated that its technical test, with its seven indicators, will permit reasoned factual determinations in individual cases.

The Commission made two clarifications regarding local distribution in the context of retail wheeling. First, it explained that even if its technical test for local distribution facilities were to identify no local distribution facilities for a specific transaction, states have authority over the service of delivering electric energy to end users. Second, the Commission explained that through their jurisdiction over retail delivery services, states have authority not only to assess retail stranded costs but also to assess charges for so-called stranded benefits, such as low-income assistance and demand-side management.

Thus, under this interpretation of state/federal jurisdiction, the Commission explained, customers have no incentive to structure a purchase so as to avoid using identifiable local distribution facilities in order to bypass state jurisdiction and thus avoid being assessed charges for stranded costs and benefits.

The Commission further determined that it is appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs.

In instances of unbundled retail wheeling that occurs as a result of a state retail access program, the Commission indicated that it will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[FN454] Moreover, the Commission indicated that it will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

As a means of facilitating jurisdictional line-drawing, the Commission stated that it will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, the Commission explained that, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the principles established in the Final Rule, the Commission indicated that it will defer to such classifications and/or cost allocations.

Furthermore, the Commission stated that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances. The Commission explained that when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes—a transmission component and a local distribution component. It again emphasized that the Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component. Thus, the Commission stated, the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. However, the Commission added, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a separate retail transmission tariff[FN455] to accommodate the design and special needs of such programs. In such situations, the Commission indicated that it will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by the Final Rule. In addition, the Commission indicated that ***12368** the rates must be consistent with its Transmission Pricing Policy Statement, and the guidance set forth in Order No. 888 concerning ancillary services.[FN456]

The Commission also expressed concern, just as it did with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, the Commission reaffirmed its conclusion that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. Moreover, the Commission indicated that it will address these transactions on a case-by-case basis.

Rehearing Requests

Oppose Commission Assertion of Jurisdiction Over Unbundled Retail Transmission

Several state commissions indicate that, recognizing that the case law is not dispositive concerning the question of unbundled retail transmission services (either because the cases do not involve the transmission of power to retail customers or "fence off" local distribution from federal regulation), at least one court (Wisconsin-Michigan Power Company v. FPC, 197 F.2d 472 (7th Cir. 1952), cert. denied, 345 U.S. 934 (1953)) explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services.[FN457] Thus, they argue, the Commission should apply the wholesale versus retail analysis to the question of unbundled retail transmission.

IL Com asserts that retail transmission by a public utility directly to an end user has always (even before the FPA was enacted) been subject to regulation by the states. It contends that no change in law has occurred which justifies the Commission's claim of expanded jurisdiction. Moreover, it disagrees with the Commission's conclusion that the unbundled delivery by the previous public utility generation supplier directly to an end user is in interstate commerce. It argues that the FPA was never intended to disturb the jurisdiction of state regulators that existed prior to its passage and that retail transmission of electric energy by a public utility to an end user was under state jurisdiction before the Attleboro decision and has remained under state jurisdiction in the over sixty years following Attleboro. Even after unbundling, according to IL Com, transmission to a retail customer still involves a retail sale of transmission.

NARUC and VA Com assert that the legislative history provides little support for the Commission's conclusion that the act of unbundling generation from delivery serves to shift jurisdiction from a state commission to the Commission. If anything, they contend, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services. They assert that the Commission should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer are subject to the jurisdiction of the state commission regulating the utility, regardless of the identity of the party generating or reselling the power or the facilities used to transport the power.

NARUC asserts that the Commission did not address a point raised in NARUC's reply comments as to how the removal of generation serves to unbundle the retail delivery function into separate transmission and distribution services. It maintains that the Commission simply assumes that a resulting transmission transaction is created when power is sold to a retail consumer by someone other than the utility delivering the power.[FN458]

MI & NH Coms ask the Commission to vacate those portions of the Rule that find that the Commission has jurisdiction over the transmission component of an unbundled retail sale in a local retail wheeling transaction. They assert that the Commission should confine its activity to wholesale transactions or those interstate transactions that do not implicate matters of local concern. They argue that the dual federal/state regulatory scheme establishes that Congress' intent is that state regulation of retail wheeling is not preempted by federal law as established in FPA section 201. They oppose unnecessary federal intrusion into local matters under a one-size-fits-all approach and assert that the retail wheeling initiatives in New Hampshire and Michigan are tailored to the unique utility environment in each state.

Central Illinois Light argues that unbundling of retail electric service does not change the states' longstanding jurisdiction over retail electric service and local distribution, even when that service involves the use of transmission in interstate commerce. It asserts that 201(b)(1) ("transmission of electric energy in interstate commerce") cannot be read in a vacuum.

MN DPS & MN Com and OH Com assert that the Commission should have no role in the regulation of retail services, be they bundled or unbundled. They argue that, in refusing to grant the Commission authority over retail wheeling, Congress left jurisdiction over retail electric service to the states. They conclude that the Final Rule contains insufficient legal and/or policy justification for the Commission's assertion of jurisdiction over unbundled retail transmission services.

MN DPS & MN Com assert: "FERC bases its usurpation of state authority over retail transmission rates on its claim that balkanization would occur without the assertion of FERC authority. Therefore, the parties are entitled to rehearing so that this essential issue can be further analyzed." (MN DPS & MN Com at 1-3).

FL Com argues that the Commission has not justified why the act of unbundling prices expands the Commission's jurisdiction into retail marketing areas. It argues that Section 212(g) of the FPA has the effect of prohibiting the Commission from usurping existing state jurisdiction over retail transmission service, whether bundled or unbundled. According to FL Com, FERC's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. It supports wheeling in jurisdiction for state commissions and wheeling out and wheeling through jurisdiction for the Commission.

IN Com opposes federalization of retail wheeling transactions within a state's boundaries as contrary to the FPA's legislative history and case law.

NJ BPU asserts that by claiming jurisdiction over unbundled retail transmission, the Commission is creating a disincentive for states to implement retail access because, by ordering retail access, the states may be relinquishing their jurisdiction over unbundled retail transmission terms and conditions—jurisdiction that they would maintain under a bundled scenario.[FN459] PA Com argues that the Commission does not have the authority ***12369** to order retail wheeling and that the jurisdictional formula is challengeable on engineering and legal grounds. It concludes that the Commission does not have jurisdiction over unbundled interstate retail transmission service. PA Com notes that the 1996 House and Senate hearings have raised the question whether the Commission has the statutory authority to restructure the electric industry. PA Com questions the Commission's definition of the "traditional tasks of state and federal regulators" on the basis of section 201(b) of the FPA, the Supremacy Clause, and the Tenth Amendment of the U.S. Constitution.

Support Broader Assertion of Jurisdiction by the Commission Over Retail Wheeling

NY Utilities declare that the Commission has jurisdiction over retail wheeling from the source to the load, but does not have jurisdiction over transmission in bundled retail service. They assert that the Commission's reliance on state jurisdictional local distribution as a predicate to abstain from allowing retail wheeling stranded cost recovery is without foundation. They further assert that a unique element that sets local distribution apart from transmission is not the size of the facility or the length of travel, but that transportation is bundled with a retail sale. According to NY Utilities, the plain meaning of the FPA shows that local distribution is bundled retail service. They claim that the legislative history, to the extent necessary, and court cases support FERC jurisdiction over all aspects of retail wheeling, but makes clear that the Commission cannot regulate bundled retail service. They add that the NGA also demonstrates that local distribution means bundled retail service.

Commission Conclusion

In concluding that this Commission has exclusive jurisdiction over the rates, terms and conditions of unbundled retail transmission by public utilities in interstate commerce, the Commission in Order No. 888 thoroughly examined the statutory language of the FPA and its legislative history, and relevant FPA and NGA case law. While the state commissions on rehearing would like us to draw a bright line that gives them, to varying degrees, jurisdiction over retail interstate transmission by public utilities, no party on rehearing has raised any legislative history or case law that was not previously considered and that would support the proposition that states have jurisdiction over any unbundled transmission in interstate commerce. As explained below, we reaffirm our jurisdictional interpretation on rehearing and believe that it is supported by the recent decision in United Distribution Companies v. FERC.[FN460]

Many of the rehearing arguments focus on the fact that states historically (even prior to the FPA) regulated retail transmission insofar as it was a component of bundled electric service to an end user, and they argue that by asserting jurisdiction over unbundled retail transmission, the Commission is somehow "taking away" jurisdiction the states previously had. The flaw in these arguments is their inherent assumption that jurisdiction over transmission service turns upon the question of whether the transmission service is being provided for "wholesale" or "retail" power sales. That is not the case. The question of jurisdiction rather turns upon the extent of the Commission's exclusive jurisdiction over transmission in interstate commerce under the FPA. The fact that states historically regulated most retail transmission service as a part of a bundled retail power sale is not the result of a legal requirement; it is the practical result of the way electricity has historically been bought and sold. However, the shape of power sales transactions is rapidly changing. Rather than claiming "new" jurisdiction, the Commission is applying the same statutory framework to a business environment in which, as discussed below, retail sales and transmission service are provided in separate transactions.

In the past, retails ales occurred almost exclusively on a bundled basis (i.e., the same entity provided a delivered product called electric energy and transmission was part and parcel of that product). The FPA clearly reserves the right to regulate retail sales of electric energy to the states. As we explained in the Final Rule, however, in today's markets, and increasingly in the future as more states adopt retail wheeling programs, retail transactions are being broken into products that are being sold separately: transmission and generation. Moreover, these products are being sold increasingly by two or more different entities. For example, a transaction may involve transmission service from one or more transmission providers who move power from a distant generation supplier, over the interstate transmission grid, to an end user. Because these types of products and transactions were not prevalent in the past, the jurisdictional issue before us did not arise and, contrary to IL Com's argument, the Commission cannot be viewed as "disturbing" the jurisdiction of state regulators prior to and after the Attleboro case.[FN461]

As we also explained in the Final Rule, the legislative history of the FPA and the relevant case law similarly reflect the historical market structure in which electricity and transmission generally were bought on a bundled basis.[FN462] Today's unbundled world simply was not contemplated and the cases do not resolve dispositively this jurisdictional issue. The case law focuses primarily on the bright line between wholesale sales and retail sales of energy, and transmission in interstate as opposed to intrastate commerce. It does not address unbundled retail interstate transmission.[FN463] We therefore have interpreted the case law in light of changed circumstances and have relied in the first instance on the plain wording of the statute. We find compelling that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce without qualification; unlike our jurisdiction over sales of electric energy, which section 201 specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission.

Since the time Order No. 888 issued, the D.C. Circuit has addressed a similar issue in interpreting section 1(b) of the NGA, the provision that parallels section 201(b) of the FPA. Under section 1(b), the Commission's jurisdiction does not apply "to the local distribution of natural gas or to the facilities used for such distribution." Similarly, under section 201(b) of the FPA, the Commission shall not have jurisdiction, except as specifically provided, "over *12370 facilities used for the generation of electric energy or over facilities used in local distribution * * *" In responding to arguments regarding the scope of state authority over "local distribution" of natural gas, the court distinguished between bundled and unbundled sales:

States have been—and are still—permitted to regulate LDCs' bundled sales of natural gas to end-users because those transactions include transportation over local mains and the retail sales of gas. In contrast, states have never regulated the terms and conditions of interstate pipeline transportation. When the gas sales element is severed—i.e., unbundled—from the transactions, FERC retains jurisdiction over the interstate transportation component." [United Distribution Companies, 88 F.3d at 1153 (footnote omitted) (emphasis in original).]

The court's reasoning is also applicable to and supports our jurisdictional determination in Order No. 888.
Several state commissions point to section 212(h) of the FPA and argue that Congress, in refusing to grant the Commission authority to order retail wheeling, left all jurisdiction over retail transmission to the states. We disagree. What Congress did in section 212(h) was to prohibit us from ordering transmission directly to an ultimate consumer. We readily recognize and respect this prohibition. However, the ability to order retail wheeling is a separate issue from whether we have jurisdiction over the rates, terms and conditions of retail wheeling in interstate commerce that is ordered by a state or that is provided voluntarily. Congress, in enacting section 212(h), did nothing to modify our jurisdiction under sections 201, 205 and 206 over the rates, terms and conditions of interstate transmission by public utilities.

Similarly, we reject FL Com's arguments that section 212(g) of the FPA prohibits the Commission from asserting any jurisdiction over unbundled retail transmission. Section 212(g) prohibits the Commission from issuing an order that is inconsistent with any state law that governs retail marketing areas of electric utilities. As we stated in the Final Rule, while our jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. We also reject arguments by the FL Com that this Commission's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. This argument is flatly contrary to the longstanding interpretation of the FPA by the United States Supreme Court. [FN464]

Commission's Seven Factor Test
IL Com argues that the Commission should withdraw its technical test. It contends that retail wheeling jurisdiction should follow function and that the function served by public utility facilities in providing retail service does not change upon the unbundling of service to retail customers. According to IL Com, Commission jurisdiction would extend to the service of delivering electric energy by a public utility to wholesale customers, regardless of the nature and extent of the public utility's facilities used to make that delivery. Similarly, it asserts, state jurisdiction would extend to the service of delivering electric energy by a public utility directly to retail customers, regardless of the nature and extent of the public utility's facilities used to make that delivery.

NARUC argues that the seven-factor test does not result in the bright line discussed in FPC v. Southern California Edison Company, 376 U.S. 205 (1964). The facility-by-facility categorization of utility systems on a company-specific basis, it asserts, is hardly consistent with the Court's decision to make case-by-case analysis unnecessary.

OH Com asserts that the seven factors provide no useful insight into the nature of local distribution service. It adds that reliance upon technical tests to determine local distribution lacks legal foundation. It further contends that the jurisdictional bright line established by Congress focuses upon the nature of the transaction, not the functional or technical characteristics of a particular wire, in determining whose jurisdictional authority attaches to a particular transaction and facilities. It concludes that the Commission should adopt the Ohio-proposed retail marketing area "wheeling in" jurisdictional approach.

PA Com contends that the Commission's seven indicia are not acceptable measures of local distribution and challenges each factor.

NH & MI Coms declare that the criteria for distinguishing transmission facilities from local distribution facilities should not be limited to the seven given in the Rule, but should allow consideration of any other relevant criteria for separating local concerns from matters legitimately federal in nature.

NJ BPU argues that the engineering-driven definition does not resolve many of the hazy areas. To the extent that the seven factors do not reflect or cannot be reconciled with the particular circumstances, it contends that the states may be hamstrung in their ability to make reasoned decisions that comport with Order No. 888.[FN465]

Similarly, NY Com argues that five of the seven factors (1, 2, 4, 6, and 7) are not accurate when applied to large metropolitan areas and remote rural areas. It asserts that local distribution facilities are not necessarily close to retail customers and the assumption that local distribution facilities are primarily radial in character fails to account for network systems. It adds that reconsignment or transportation of power to different markets can and does occur at the local distribution level. It further adds that the presence of meters is not a discerning characteristic of where interstate transmission ends and local distribution begins; meters are frequently not part of the transmission/local distribution interface. Nor, according to NY Com, are local distribution systems necessarily of reduced voltage. Instead of the 7 criteria, NY Com argues that the Commission should adopt a functional measure of local distribution based on factors 3 and 5 (interstate transmission ends and local distribution begins where electricity flows into a comparatively restricted geographic area and does not flow back out of that area and the power is consumed in that area) and on the traditional classification of the facilities by the state regulatory body (or what the utility has traditionally classified as local distribution).

Commission Conclusion

Several parties on rehearing do not like the seven-factor technical test for local distribution facilities that was set forth in Order No. 888. That test takes into account both technical and functional characteristics of the transaction involved. The parties on rehearing propose instead a variety of bright line tests. For example, IL Com wants state jurisdiction to extend to the "service" of delivering electric energy to retail customers, which it would define to give it jurisdiction regardless of the ***12371** nature and extent of the facilities used to make the delivery. OH Com proposes that the Commission adopt a retail marketing area "wheeling in" jurisdictional approach which would give it jurisdiction over facilities within territorial boundaries.

In response, we do not interpret the FPA to permit us in effect to rewrite the statute to give states jurisdiction over interstate transmission services. Moreover, we reject arguments of OH Com that our seven-factor test lacks legal foundation, and arguments of NARUC that we are somehow bound to develop a bright line test. While Congress established a jurisdictional bright line between wholesale and retail sales of energy, there is no such bright line that we can divine with regard to transmission and local distribution facilities. The Supreme Court, in both Colton and CL&P,[FN466] has instructed us that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. The seven factors will permit us to undertake this fact-specific determination.

We acknowledge the concerns raised by several state commissions that the seven-factor test does not, as NJ BPU puts it, resolve many of the hazy areas, and that there may be other factors that should be taken into account in particular situations. The seven-factor test is intended to provide sufficient flexibility to take into account unique local characteristics and historical usage of facilities used to serve retail customers. We specifically stated in the Final Rule that we will consider jurisdictional recommendations by states that take into account other technical factors that states believe are appropriate in light of historical uses of particular facilities. Moreover, we will defer to facility classifications and/or cost allocations that are supported by state regulatory authorities. For example, in the ongoing California electric utility restructuring proceeding, the Commission deferred to the State PUC's recommendations regarding the split between state jurisdictional local distribution facilities and Commission-jurisdictional transmission facilities.[FN467]

Oppose Transmission of Public Utility Purchases for Sale at Retail

IL Com objects to the transmission unbundling requirement if it is intended to require public utilities to take transmission services under their own FERC tariffs for purchases of power intended for distribution by the public utility to retail customers. According to IL Com, a distinction must be made between the public utility's use of its transmission system in cases in which the public utility purchases wholesale power for sale for resale, and cases in which the public utility purchases wholesale power to serve native load retail customers. It argues that the Commission cannot legally regulate, or place conditions on, the manner in which a utility uses its transmission system to make sales of electric energy at retail. It contends that the Commission must exempt public utility power purchases for sale at retail from the unbundling requirement. It recommends that the Commission insert the words "for sale for resale" after the word "purchases" in section 35.28(c)(2) and after the word "purchase" in section 35.28(c)(2)(i).

Commission Conclusion

The Commission rejects arguments of IL Com that if unbundled retail wheeling occurs either voluntarily or as a result of a state retail program, we cannot require the utility to take service under its own transmission tariff for sales to retail customers. This requirement is a term and condition of unbundled retail interstate transmission service and, as explained above, therefore is within our exclusive jurisdiction. Additionally, this should not in any way infringe on state retail programs or service to retail customers. Rather, it ensures that non-discriminatory transmission services are provided to all potential retail power competitors.

Further, as stated previously in Section IV.C.1.b (Transmission Providers Taking Service Under Their Tariff), we clarify that a transmission provider does not have to "take service" under its own tariff for the transmission of power that is purchased on behalf of bundled retail customers.

Oppose Buy-Sell Transaction Analysis

PA Com asserts that there is a potential for jurisdictional conflict with respect to buy-sell transactions that is a direct consequence of the technical-functional test (which PA Com challenges).

IL Com argues that states have exclusive authority to regulate buy-sell arrangements as bundled retail sales. It further argues that the Commission cannot make a bundled retail sale into an unbundled retail sale simply by characterizing it as the functional equivalent of an unbundled retail sale; by re-characterizing them the Commission is effectively ordering the unbundling of buy-sell arrangements. It asserts that buy-sell arrangements on the electric side are not an end run around clear federal jurisdiction and that the Commission should withdraw its assertion of jurisdiction over the retail transmission component of unbundled retail sales.

VT DPS contends that the Commission's rationale is flawed: "FERC's analysis rests on the same very shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies." According to VT DPS, all retail transactions are subject to state jurisdiction and asks the Commission to clarify that the Commission defines buy-sell as it did in the NOPR, but also acknowledge that it has no jurisdiction over such arrangements.

IN Com asserts that in the absence of any record of abusive and undermining actions by states under the guise of buy-sell arrangements, there is not even a remedial justification to touch buy-sell transactions. It contends that a difference between the FPA and the NGA warrants different treatment—the FPA exempts from FERC jurisdiction local distribution and transmission of electric energy in intrastate commerce. By redefining interstate transmission, IN Com claims that the Commission proposes to do away with the meaning history has accorded to a variety of transactions previously considered wholly intrastate in nature. According to IN Com, states should be allowed to experiment with and allow different forms of buy-sell transactions as part of the evolving marketplace.

Commission Conclusion

Four parties (PA Com, IL Com, VT DPS and IN Com) have raised concerns regarding the Commission's determination that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third party. The Commission reiterates that we will have to address these situations on a case-by-case basis. We disagree with IL Com that States have exclusive authority to regulate the interstate transmission component of buy-sell transactions. Similarly, we deny the VT DPS request that we acknowledge no jurisdiction over such arrangements. The fact remains that these arrangements could be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. We reserve our authorities to ensure that public utilities and their ***12372** customers are not able to circumvent non-discriminatory transmission in interstate commerce. In response to VT DPS' contention that the Commission's analysis here rests on the same shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies, we note that the D.C. Circuit recently affirmed the Commission's assertion of jurisdiction over buy/sell arrangements under the Natural Gas Act.[FN468]

State Jurisdiction Over the Service of Delivering Electric Energy to End Users

Rehearing Requests

IL Com states that it is far from clear what FERC contemplates by the "service" of delivery of electric energy by a delivering utility in the retail wheeling transaction. It is equally unclear to IL Com whether the "service" to which Order No. 888 refers is a public utility activity over which state regulators would have jurisdiction. IL Com argues that it is the Illinois legislature, not FERC, that determines whether IL Com can regulate something called "delivery service."[FN469]

MO/KS Coms ask the Commission to clarify the meaning of the statement that even when the test for local distribution facilities identifies no local distribution facilities, the Commission believes that states have authority over the service of delivering electric energy to end users. According to MO/KS Coms:

The authority to shop at retail and to sell at retail do not exist in the FPA. If the Commission's goal is to recognize the States' authority to establish conditions on retail competition, it need only acknowledge the State jurisdiction to establish the opportunity to shop and sell at retail. If this is what the Commission is seeking to accomplish by its discussion of 'delivery service,' then we support the Commission.[FN470]

Coalition for Economic Competition asserts that the Commission failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, and that the local regulatory commission may have no jurisdiction over either the sale or the transmission of the energy.

Commission Conclusion

Several parties ask us to clarify our conclusion that even when the seven-factor test for local distribution facilities does not identify local distribution facilities, we believe states have authority over the "service" of delivering electric energy to end users. We clarify that states have the authority to determine the retail marketing areas of electric utilities within their jurisdictions, and the end user services that those utilities must provide, but we did not in Order No. 888 intend to opine on the extent of authority given by state legislatures to their state commissions. Rather, our statement regarding state authority over the "service" of delivering electric energy is intended to recognize the historical and local nature of delivering power to end users and the states' legitimate concerns and responsibilities in regulating local matters.

Deference to States

Rehearing Requests

Support Broader Deference
NARUC and IL Com argue that the Commission should not simply defer to state recommendations concerning the application of the seven-factor test or the recovery of stranded costs, but should conclusively rely on the findings by state commissions.

NY Com argues that the Commission should not limit deference to instances in which states order retail wheeling, but should defer to all state commission recommendations regarding the definition of local distribution facilities.

FL Com asserts that the Rule fails to say where deference will be given. It argues that the Rule should state that when a state commission has held a proceeding on matters related to the requirements of the Rule, the Commission shall give deference to the state commission decisions. Moreover, it asserts that the Commission should codify the deference standard: "When a state commission has held a proceeding on matters related to the requirements of this rule, the Commission shall give deference to the state commission decisions." (FL Com at 7-9).

The commitment to defer to a state regulatory commission or agency, argues NE Public Power District, should be clarified with respect to utilities located in Nebraska, which has no such commission or agency. NE Public Power District assumes that deference will be accorded to decisions of NE Public Power District's Board of Directors; if not, it asks the Commission to clarify.

PA Com asks the Commission to clarify what a state regulatory agency must demonstrate to secure deference and to define the term "consult." PA Com states that, in discussing the seven indicia, the Commission states that it will "consider" jurisdictional recommendations by states, which PA Com asserts is much different from deference. It also asserts that the Commission must clarify what it will do if a utility's classifications and/or cost allocations are not supported by state regulatory authorities.

Oppose Deference to State Authorities
TANC argues that the Commission erred in deferring to state regulatory authorities in drawing jurisdictional lines for local distribution facility classifications and/or cost allocations. According to TANC, the Commission unlawfully and unnecessarily abdicated its jurisdiction under the FPA (citing New England Power Co. v. New Hampshire, 455 U.S. 331, and Nantahala Power and Light Co. v. Thornburg, 476 U.S. 953). With respect to ISOs, it asserts that the Commission should not defer to state authority in making determinations with respect to classifications of facilities.

Commission Conclusion
In response to NARUC and IL Com's arguments that this Commission should not simply defer to state commissions regarding application of the seven-factor test but instead should conclusively rely on the findings of state commissions, we believe this is inconsistent with the case law which states that local distribution it is a matter of fact for the Commission to determine as an original matter.[FN471] Additionally, we have an independent obligation to ensure that we are fulfilling our responsibilities under the FPA to regulate facilities that are used in interstate commerce. We cannot delegate our jurisdiction. However, we intend to provide broad deference to states in determining what facilities are Commission-jurisdictional transmission facilities and what facilities are state-jurisdictional local distribution facilities, so long as our comparability principles are not compromised and we are able to fulfill our responsibilities under the statute.

We reject FL Com's suggestion that we codify the deference standard. This is neither necessary nor appropriate. In response to NE Public Power District's request that we clarify to whom we would give deference in Nebraska, we clarify that because Nebraska does not have an electric regulatory commission or agency, there is no appropriate regulatory entity to whom our deference standard would apply; accordingly, we will address the transmission/local ***12373** distribution issue for Nebraska without giving deference to any particular entity. In response to PA Com's request that we clarify what we will do if a utility's classifications and/or cost allocation proposals are not supported by state regulatory authorities, we will make a determination based on the factual record before us in a particular case, taking into account the views of the state regulatory authority.

TANC has argued that we have unlawfully abdicated our jurisdiction by deferring to state recommendations. TANC confuses delegation of jurisdiction, which we cannot do, with willingness to defer to states based on their application of criteria that we have provided. Even in the cases in which the Commission defers to states' views, we will still independently evaluate all material issues and proceed only where substantial evidence supports the states' views. The Commission clearly can entertain requests for deference in these circumstances.

J. Stranded Costs

As indicated in our prior discussion in Section IV.A.5, there are two major overlapping transition issues that arise as a result of this rulemaking: stranded cost recovery and how to deal with contracts entered into under the prior regulatory regime. We here address stranded cost recovery and, as in the prior discussion, we believe it is important to explain the general context in which our stranded cost determinations have been made before addressing the various rehearing requests on this issue.

In Order No. 888, the Commission removed the single largest barrier to the development of competitive wholesale power markets by requiring non-discriminatory open access transmission as a remedy for undue discrimination. This action carries with it the regulatory public interest responsibility to address the difficult transition issues that arise in moving from a monopoly, cost-based electric utility industry to an industry that is driven by competition among wholesale power suppliers and increasing reliance on market-based generation rates. The most critical transition issue that arises as a result of the Commission's actions in this rulemaking is how to deal with the uneconomic sunk costs that utilities prudently incurred under an industry regime that rested on a regulatory framework and a set of expectations that are being fundamentally altered.

The Commission determined in Order No. 888 that it must address stranded costs, and that it must do so at an early stage—particularly in light of the lessons learned from our experience with similar issues in the natural gas area. We noted that when we did a similar restructuring in the gas industry, the D.C. Circuit invalidated the Commission's efforts precisely because the Commission had failed to deal with the stranded cost problem in a satisfactory manner.[FN472] We explained that, based on the lesson of AGD, the Commission cannot change the rules of the game without providing a mechanism for recovery of the costs caused by such regulatory-mandated change.

Since the time Order No. 888 issued, we have been provided with additional guidance from the court in the natural gas area, which has further helped to inform our decisions here. In its decision on review of Order No. 636,[FN473] the D.C. Circuit upheld the Commission's decision to allow the recovery of gas supply realignment costs. In so doing, the court, while questioning a specific feature of the stranded cost recovery mechanism employed in Order No. 636, has nevertheless again reaffirmed the basic principle that stranded cost recovery is an appropriate component of a regulatory policy aimed at accomplishing a fair and reasonable transition to competitive markets. The question as to the Commission's ability to allow the recovery of stranded costs has been laid to rest.

The task before the Commission in this rulemaking is thus to determine how best to meet its responsibility to address the costs of the transition to a competitive industry, particularly insofar as those costs are stranded, or in effect rendered unrecoverable, as a result of the transmission access required by us under the FPA.[FN474] As the rehearing arguments demonstrate, there is no consensus on how the Commission should address the stranded cost issue. In fact, petitioners are at polar extremes as to what the Commission should do regarding stranded costs. Some argue that the Commission has gone too far in permitting utilities to seek recovery of stranded costs, whether such costs are associated with wholesale requirements contracts, with retail-turned-wholesale customers, or with retail customers that obtain retail wheeling.[FN475] Others argue that the Commission has not gone far enough and that it must broaden the scope of stranded cost recovery permitted under the Rule. Indeed, some would have us be the guarantor for recovery of all uneconomic costs that might be stranded in the move to more competitive markets, no matter how tenuous the nexus to this Rule, and irrespective of state-Federal jurisdictional complexities. Some support the Commission's decision to recover stranded costs directly from the departing customers. Others would prefer that the Commission require utilities to absorb a portion of their stranded costs or that the Commission spread the burden of stranded costs among all of the utility's customers. Some object that the Commission's approach to stranded costs in the electric industry is different from that adopted in the gas industry. Some entities support the Commission's revenues lost approach for measuring a departing customer's stranded cost obligation. Others propose different methods for computing stranded costs.

Given the plethora of positions that entities have raised both initially and on rehearing concerning stranded costs, the Commission has taken a careful, measured approach with regard to stranded cost recovery. The Commission has balanced a number of important interests in order to achieve what it believes will be a fair and orderly transition to competitive markets. These interests include the financial stability of the electric utility industry, upholding the regulatory bargain under which utilities made major capital investments, and not shifting costs to customers that had no responsibility for causing those costs to be incurred. The Commission also has adopted an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of stranded cost recovery from retail customers, recognizes state commission ***12374** jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures.

The balancing of interests and considerations described above is reflected in the following central components of the Rule's stranded cost provisions, which are reaffirmed herein.[FN476] First, the Commission has determined that the most reasonable, legally supportable approach is one that permits utilities to seek recovery of wholesale stranded costs under this Rule (whether the stranded costs are associated with a departing wholesale requirements customer or with a retail-turned-wholesale customer) only in those cases in which there is a direct nexus between the availability and use of Commission-required transmission access[FN477] and the stranding of costs. In order for the utility to be eligible to seek recovery of stranded costs from a departing customer, the customer must have obtained access to a new generation supplier through the use of the former supplying utility's Commission-required transmission tariff (i.e., its open access tariff or a tariff ordered pursuant to FPA section 211), not through the use of another utility's transmission system.

Other cost recovery issues are more appropriately addressed outside the context of this Rule. For example, the Rule is not intended to apply to costs associated with the normal risks of competition, such as self-generation, cogeneration, or loss of load, that do not arise from the new, accelerated availability of Commission-required transmission access. If a customer leaves its utility supplier by exercising options that could have been undertaken prior to mandatory transmission under Order No. 888 or the Energy Policy Act, or that do not rely on access to the former seller's transmission, there is no direct nexus to Commission-required transmission access and thus no opportunity for stranded cost recovery under the Rule.

Second, the Commission has limited the opportunity to seek stranded cost recovery under the Rule primarily to two discrete situations: (1) Costs associated with customers under wholesale requirements contracts executed on or before July 11, 1994 (referred to in the Rule as "existing wholesale requirements contracts") that do not contain an exit fee or other explicit stranded cost provision; and (2) costs associated with retail-turned-wholesale customers. With regard to the existing wholesale requirements contracts, the Commission also has made a finding that it is in the public interest to permit amendments to add stranded cost provisions to these contracts, even if they contain Mobile-Sierra clauses, if case-by-case evidentiary burdens are met. We do not interpret the Mobile-Sierra public interest standard as practically insurmountable in extraordinary situations such as this one where historic statutory and regulatory changes have converged to fundamentally change the obligations of utilities and the markets in which they and their customers will operate.

Third, Order No. 888 does not guarantee that a utility will be allowed to recover stranded costs. Rather, it provides an opportunity for such recovery. To be eligible to recover stranded costs from a departing customer in a particular case, the utility must demonstrate that it incurred costs to provide service to the customer based on a reasonable expectation of continuing service to that customer beyond the contract term.[FN478] In the case of stranded costs associated with wholesale requirements contracts customers, if the contract contains a notice of termination provision, that provision is strong evidence that the parties were aware that at some point in the future the customer might seek to find another supplier. Therefore, there is a rebuttable presumption of no reasonable expectation, and therefore no opportunity for stranded cost recovery unless the utility can overcome the presumption.

The Commission has concluded that direct assignment of stranded costs to the departing customer (through either an exit fee or a surcharge on transmission) is the appropriate method for recovery of stranded costs under the Rule. In reaching this conclusion, the Commission carefully weighed the arguments supporting direct assignment of stranded costs against those supporting a more broad-based approach, such as spreading stranded costs to all transmission users of a utility's system, and also took into account the fact that we applied a different approach in the natural gas area. The central considerations that support a direct assignment approach in the electric industry are that the approach follows the traditional regulatory concept of cost causation, it avoids shifting costs to customers that had no responsibility for causing them to be incurred or for causing them to be stranded, and it is still possible to apply such an approach at this stage of the industry's evolution.

There is no question that, without the stranded cost recovery mechanism, some customers would be far more likely to switch to lower-cost suppliers and enjoy sooner the benefits of a competitive power market. But, as detailed in Order No. 888, such an approach may result in higher costs for other customers. We thus have had to balance the potential for earlier benefits for some customers against other public interest considerations, most particularly the need to provide a fair mechanism by which utilities can recover the costs of past investments under traditional regulatory concepts of prudently incurred costs and cost causation. The result is not to deny competitive advantages, but only to delay their full realization for some customers so that all customers ultimately will benefit.

While Order No. 888's cost causation approach is different from the Order No. 636 cost spreading approach that was affirmed in the United Distribution Companies case, we believe it is the preferable approach given the early stage of the electric utility's competitive transition. We do not read the court's opinion as precluding the Commission from adopting a direct assignment approach in Order No. 888, particularly where, as here, the Commission has fully explained and justified the reasons for following traditional cost causation principles. In addition, although the United Distribution Companies court remanded for further consideration (in light of Order No. 636's cost spreading approach) the decision not to require any pipeline absorption of gas supply realignment costs, the Commission has fully explained how its decision in Order No. 888 not to require any utility absorption of stranded costs is consistent with its decision to follow traditional cost causation principles. With respect to the fundamental conclusion that utilities should be permitted an opportunity to recover their prudently incurred costs, Order No. 888 is fully consistent with Order No. 636. Although the Commission in Order No. 888 chose a direct assignment method (rather than the cost-spreading ***12375** approach in Order No. 636) for purposes of allocating stranded cost responsibility among customers, the approach used by the Commission in Order No. 888 is not governed by decisions in Order No. 636, but in either event the Commission must demonstrate that its choice of methods is based on reasoned decision-making.

In considering the stranded cost issues that may arise in the transition to competitive markets, the Commission also has taken cognizance of significant changes involving retail customers and the stranded cost issues that arise as retail customers convert to wholesale customer status (e.g., through municipalizations) in order to obtain the open access afforded by Order No. 888, or as they obtain retail wheeling required by state commissions. These situations involve new and complex jurisdictional issues and represent the bulk of potential stranded costs facing the industry. We believe it is important to clarify the Commission's decisions as to when it will entertain requests for stranded cost recovery in these situations, and our reasons for doing so.

The Commission's determination that it, rather than the states, should be the primary forum for addressing stranded costs associated with a retail-turned-wholesale customer [FN479] is limited to those cases in which there is a direct nexus between the availability and use of Commission-required transmission access and the stranding of costs. We believe we have both the authority and the obligation to provide an opportunity for stranded cost recovery in these situations because the bundled retail customer would not be able to obtain access to the new supplier but for the Commission's order requiring transmission. The creation of a new wholesale entity to purchase power on behalf of retail customers would not, by itself, trigger stranded costs. In the absence of transmission access from the historical supplier of the retail customers, the new entity would have to remain on the historical supplier's generation system because it would have no way to reach other power suppliers, and stranded costs would not occur.[FN480] Therefore, there is a causal nexus between the stranded costs and the availability and use of the tariff services required by the Commission.[FN481] Moreover, because of this causal nexus between the use of a jurisdictional utility's Commission-required transmission tariff and the potential for foregone revenues by that jurisdictional utility as a result of the Commission-required access, the stranded costs associated with a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In contrast, in the situation in which a bundled retail customer obtains retail wheeling, stranded costs are directly caused by the availability and use of unbundled retail services required by the state commission, not this Commission.[FN482] Thus, the Commission believes that states, not the Commission, should be the primary forum for costs associated with a bundled retail customer that obtains retail wheeling. The Commission's decision to entertain requests to recover stranded costs caused by retail wheeling in only a limited circumstance (where the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on a policy decision by this Commission that it will step in to fill a regulatory "gap" that could result in no effective forum in which utilities would have an opportunity to seek recovery of prudently incurred costs.

Finally, after considering various proposals regarding how stranded costs should be calculated, and reviewing the arguments of petitioners on rehearing, the Commission continues to believe that the revenues lost approach is the fairest and most efficient way to determine the amount of stranded cost assigned to a departing customer during the transition to a competitive wholesale bulk power market. The Commission has rejected an asset-by-asset approach as overly complicated and costly.

We respond below to the specific arguments raised on rehearing and elaborate on the above determinations.

1. Justification for Allowing Recovery of Stranded Costs

In Order No. 888, the Commission concluded that utilities should be given the opportunity to seek recovery of legitimate, prudent and verifiable stranded costs associated with a limited set of wholesale requirements contracts executed on or before July 11, 1994.[FN483] We stated that utilities that entered into contracts to make wholesale requirements sales under an entirely different regulatory regime should have an opportunity to recover stranded costs that occur as a result of customers leaving the utilities' generation systems through Commission-jurisdictional open access tariffs or FPA section 211 orders to reach other power suppliers. We explained that utilities that made large capital expenditures or long-term contractual commitments to buy power years ago to supply their customers should not now be held responsible for failing to foresee the actions this Commission would take to alter the use of their transmission systems in response to the fundamental changes that are taking place in the industry. We found that recent significant statutory and regulatory changes are central to the circumstances that now place at risk the recovery of past investment decisions of utilities. We indicated that we will not ignore the effects of these changes as we fashion policies that will govern possible recovery of these costs in the transition to an open access regulatory regime.

We stated that while there has always been some risk that a utility would lose a particular customer, in the past that risk was smaller. It was not ***12376** unreasonable for the utility to plan to continue serving the needs of its wholesale requirements customers and retail customers, and for those customers to expect the utility to plan to meet their future needs. We concluded that with the new open access transmission, [FN484] the risk of losing a customer is radically increased. If a former wholesale requirements customer or a former retail customer uses the new open access to reach a new supplier, the utility is entitled to seek recovery of legitimate, prudent and verifiable costs that it incurred under the prior regulatory regime to serve that customer. The utility, however, would have the burden of demonstrating that it had a reasonable expectation of continuing to serve the departing customer.

Rehearing Requests Opposing, or Seeking Limitations on, Stranded Cost Recovery

Several entities challenge the Commission's decision to give utilities an opportunity to recover legitimate, prudent and verifiable stranded costs. NASUCA argues that the transition to wholesale competition was underway before and apart from the NOPR. It asserts that the drivers of the developing competition include voluntary open access filings by utilities seeking mergers or market-based rate authority and section 211 of the FPA, as amended by the Energy Policy Act of 1992 (Energy Policy Act). According to NASUCA, stranded investment results from legislative, not regulatory action, and the stranded cost issue does, and would, exist without the Open Access Rule. It contends that an acceleration of the competitive wholesale transformation does not change its nature or origins. NASUCA also contends that the issuance of the Open Access Rule does not justify stranded cost recovery on "regulatory compact" grounds because it is not a fundamental change.

Other entities object that there is no basis for the Commission to impute an extra-contractual obligation to serve wholesale requirements customers.[FN485] These entities argue, for example, that utilities could and should have protected themselves from any potential stranded costs through individual customer contracts.

IN Consumer Counselor and IN Consumers object that Order No. 888 attempts to transform the obligation to provide a utility with an "opportunity" for a fair return when prices are regulated into an "entitlement" to "recover legitimate, prudent and verifiable costs that it incurred under the prior regulatory regime."[FN486]

Several entities submit that the Commission has not adequately addressed the potential anticompetitive impact of stranded cost recovery.[FN487] Some argue that giving utilities the opportunity to recover wholesale stranded costs will delay the opportunity for historically captive customers to benefit from competitive alternatives.[FN488] Central Illinois Light contends that the Rule is arbitrary and capricious because it will have different impacts on different customers, which Central Illinois Light asserts will be due to accidents of circumstance rather than the conscious application of rational policy choices. IN Consumers objects that two similarly-situated customers of the utility for identical transmission services will be required to pay substantially different rates for the same service (where one previously purchased its power requirements from the utility, while the other used an alternate source of supply).

Central Illinois Light also objects that even a partial allowance of stranded costs will likely encourage predatory pricing. It says that the Commission has failed to adequately address the harm that stranded cost "subsidies" pose to low-cost utilities with little or no stranded costs. Others contend that the Rule would subvert economic efficiency by unjustly enriching utilities that have not attempted to meet the new market demands, to the detriment of those utilities that have.[FN489] According to Occidental Chemical, the Commission has made no finding that the pro-competitive goals of Order No. 888 can be accomplished in light of the costs and uncertainties presented by stranded cost recovery.

Several entities also challenge the adequacy of the factual record for allowing wholesale stranded cost recovery and argue that utilities have not provided the hard data on wholesale stranded costs that the Commission needs to justify Order No. 888. [FN490] Central Illinois Light objects that the Commission failed to note or to discuss data presented by commenters showing that only a small group of high-cost utilities need some stranded cost protection. American Forest & Paper argues that the Commission has failed to demonstrate on the record the existence of any stranded wholesale investment that was or could be caused by the transition to open access transmission.

SC Public Service Authority repeats its earlier request that the Commission deny market-based rate authority to any utility that elects to recover stranded costs from departing customers.[FN491] It objects that the Commission failed to specifically respond to its previous comments on this issue.

American Forest & Paper objects that utilities that voluntarily filed open access tariffs cannot use the stranded cost rule because their loss of customers cannot be said to have occurred only because of the Rule. It submits that only those utilities who had to be forced to offer open access transmission are being rewarded.

San Francisco asks that the Commission include "exercise of pre-existing contract rights for transmission and designation of wholesale loads" or similar language as one of the examples (listed in footnote 718) of situations for which stranded costs may not be sought. San Francisco explains that it wants to ensure that PG&E would not have any basis to argue that any load loss PG&E suffers as a result of San Francisco's designation of municipal loads would be eligible for stranded cost recovery.

Commission Conclusion

We will deny the requests for rehearing of our decision to allow *12377 utilities an opportunity to seek recovery of legitimate, prudent, and verifiable stranded costs. As we indicated in Order No. 888, we learned from our experience with natural gas that, as both a legal and a policy matter, we cannot ignore these costs. The U.S. Court of Appeals for the District of Columbia Circuit invalidated the Commission's first open access rule for gas pipelines because the Commission failed to deal with the uneconomic take-or-pay situation that many pipelines faced as a result of regulatory changes beyond their control.[FN492] That same court has subsequently affirmed the Commission's decision to allow the recovery of costs that are stranded in the transition to a competitive natural gas industry, most recently by upholding the Commission's decision in Order No. 636 to allow the recovery of gas supply realignment costs.[FN493]

Here we are faced, once again, with an industry transition in which there is the possibility that, as a result of statutory and regulatory changes beyond their control, certain utilities may be left with large unrecoverable, legitimate and prudent costs or that those costs will be unfairly shifted to other (remaining) customers. Thus, in order to satisfy our regulatory responsibilities, we must directly and timely address the costs of the transition by allowing utilities to seek recovery of legitimate, prudent and verifiable stranded costs.[FN494] While the transition to wholesale competition may have begun before the NOPR, we strongly disagree with NASUCA's claim that the Open Access Rule does not justify stranded cost recovery because an acceleration of the transition does not change its nature or origins. The driving force behind the development of wholesale competitive markets is the widespread transmission access made available through Commission-mandated transmission tariffs,[FN495] including transmission tariffs ordered pursuant to FPA section 211 and the transmission tariffs required by the Commission's Open Access Rule.[FN496] Furthermore, as explained in the Rule and as further discussed below, it is the ability of customers to obtain readily available Commission-mandated transmission access that significantly increases the potential for wholesale stranded costs.

Order No. 888 requires the functional unbundling of a public utility's wholesale services. Under the Rule, all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce were required by July 9, 1996 to file open access transmission tariffs that contain minimum terms and conditions of non-discriminatory service (or to seek waiver), and to take transmission service (including ancillary services) for their own new wholesale sales and purchases of electric energy under the open access tariffs. As a result of Order No. 888, wholesale requirements customers that previously were captive customers of their public utility suppliers (i.e., they had no choice but to take bundled sales and transmission services from their suppliers) will be able at the expiration of their contracts to take unbundled transmission service (i.e., transmission-only service) from their former suppliers in order to reach new suppliers. While in the past there has been some risk of stranded costs due to customers "leaving" a supplier's system through self-generation or perhaps municipalization, there was little or no ability to shop for alternative power such as that which will occur as a result of readily available Commission-mandated transmission access. Contrary to NASUCA's claims, Order No. 888, coupled with section 211 of the FPA, creates the opportunity, as a matter of law, for an existing wholesale requirements customer to use the transmission owner's facilities to reach a new supplier.[FN497] This leaves the former supplying utility with significant risk that it will be unable to recover costs that the utility incurred based on a reasonable expectation that it would continue to serve the departing customer.

Thus, the regulatory and statutory changes contained in Order No. 888 and in amended section 211, which will act in tandem to provide the transmission access necessary to develop the competitive wholesale markets envisioned by Congress in the Energy Policy Act, have a direct nexus to the potential for wholesale stranded costs. This nexus makes it critical that the Commission address this transition issue responsibly and equitably. Having balanced the goals of competition, the nexus between potential stranded costs and transmission access, and the regulatory bargain under which utilities invested billions of dollars in reliance on the prior regulatory regime, we believe that utilities are entitled to an opportunity to seek recovery of stranded costs and that our actions in Order No. 888 are not only legally supportable, but also represent sound public policy.

In response to those entities who argue that there is no basis for imputing an extra-contractual obligation to serve wholesale requirements customers, as we explained in Order No. 888, we believe there previously has been an implicit obligation to serve at wholesale in many cases. Such obligation is based, in large part, on the recognition that historically most wholesale requirements customers were captive and had no means of reaching alternative suppliers. The local utility supplied bundled generation and transmission services to these customers on the assumption that they would remain as customers. Accordingly, the utility had a concomitant obligation to plan to supply these customers' ***12378** continuing needs, and planned its system taking account of the wholesale load. In many cases the wholesale customers participated by supplying load forecasts. Consistent with this practical obligation to serve, the Commission viewed the supplying utility as the supplier of first resort, and did not allow a utility to terminate service without prior Commission approval. Before Order No. 888, the Commission's regulations required prior notification and approval of the proposed cancellation or termination of a wholesale requirements contract. We note that although Order No. 888 eliminates the prior notice of cancellation or termination requirement for power sales contracts executed on or after July 9, 1996 (the effective date of the Open Access Rule) that are to terminate by their own terms,[FN498] it expressly retains the prior notice of cancellation or termination requirement for any power sales contract executed before that date.

It is important to note, however, that while the stranded cost recovery provisions of the Rule are based on the implicit obligation to serve, the Rule does not guarantee any extra-contractual wholesale stranded cost recovery, much less across-the-board recovery of such costs by all public utilities. To the contrary, it provides an opportunity for such recovery only for a discrete set of requirements contracts (those executed on or before July 11, 1994 that do not contain an exit fee or other explicit stranded cost provision), and the Rule requires that a utility must meet a heavy burden of proving eligibility to recover costs in a particular case: before a departing customer is required to pay a stranded cost exit fee or transmission surcharge, the utility must demonstrate that it incurred costs to provide service to a customer based on a reasonable expectation of continuing service to that customer beyond the end of the contract.[FN499]

We believe that we adequately address in both Order No. 888 and in Section IV.J.2 below the concerns various entities have expressed as to the potential anticompetitive impact of stranded cost recovery. Although we recognize that stranded cost recovery may delay some of the benefits of competitive bulk power markets for some customers, we believe that customers as a whole will benefit from a fair and orderly transition. Indeed, we are particularly concerned that the failure to assign stranded cost responsibilities to customers that have access to alternative suppliers will leave captive customers exposed to the risk of greater cost burdens, thereby shifting to captive customers the costs that were originally incurred for the benefit of the (typically larger) customers who have the flexibility to take early advantage of competing power suppliers. Avoiding this potential cost shifting problem is an important goal of our decision to address the stranded cost problem as part and parcel of the decision to mandate open access. As we said in Order No. 888:

such transition costs must nevertheless be addressed at an early stage if we are to fulfill our regulatory responsibilities in moving to competitive markets. The stranded cost recovery mechanism that we direct here is a necessary step to achieve pro-competitive results. In the long term, the Commission's Rule will result in more competitive prices and lower rates for consumers.[FN[500]] We do not believe that allowing utilities an opportunity to seek stranded cost recovery will prevent us from achieving the pro-competitive goals of Order No. 888. To the contrary, as discussed below in Section IV.J.3, we think that it is necessary to provide utilities the opportunity to seek to recover stranded costs if we are to have a fair and orderly transition to more competitive bulk power markets. The opponents of Order No. 888's stranded cost approach argue that the transition to fully competitive bulk power markets will be slower if we allow utilities an opportunity to seek to recover stranded costs from departing customers, and with respect to some customers that may well be true. As noted earlier, some customers because of their size and limited contractual obligations with their current utility suppliers have the ability immediately to leave the system. If they are allowed to do so without paying the costs incurred to provide them expected future service, the economic attractiveness of departing the system is obviously enhanced and the benefits of competition, for these customers, obviously come sooner rather than later. However, the pace at which fully competitive markets are achieved, while important, is not the only consideration. It is the Commission's responsibility to ensure that the costs of open access are fairly assigned and that the benefits of Order No. 888's open access requirements will be fairly available to all customers. These dual goals compel us toward a balanced approach that, although perhaps delaying somewhat the benefits of competition, nevertheless ensures that all customers will share in those benefits without undermining historic principles of cost recovery upon which utilities were entitled to rely in planning their systems.

Moreover, as we explain in Section IV.J.3 below, we have carefully examined different methods of allocating stranded costs that are found to be properly recoverable, including assigning the costs directly to the departing customer or spreading the costs to all transmission users of a utility's system. We recognize that the direct assignment approach to stranded cost recovery delays competition for some customers because it attaches a price tag for customers who have the immediate ability to leave the system. However, we have identified the advantages and disadvantages of each approach and have concluded, on balance, that direct assignment is the preferable approach for both legal and policy reasons.

In response to the concerns of some entities that stranded cost "subsidies" may harm low-cost utilities with little or no stranded costs, or otherwise may unjustly enrich utilities that have not attempted to meet the new market demands to the detriment of those that have, we again emphasize the limited and transitional nature of the stranded cost recovery opportunity allowed under Order No. 888.[FN501] It is clearly not the Commission's intent that utilities with little or no stranded cost exposure be competitively disadvantaged by the Open Access Rule. Those utilities with little or no stranded costs will be similarly situated with other new suppliers in the sense that they will all ***12379** face the potential of not being able to compete immediately for certain wholesale customers who are determined to have an obligation to pay stranded costs. These customers may find it to be uneconomic to shop from new power suppliers because they may have to pay costs they caused to be incurred under the prior industry regime before they are able to switch suppliers. However, this will be during a transition period only, and only with respect to a discrete set of contracts and only where the utility meets its burden of proof with respect to a particular departing customer.

We reject as misplaced IN Consumers' argument that the Open Access Rule is discriminatory because two "similarly-situated" customers for "identical" transmission services (one who previously purchased transmission bundled with its power requirements from the utility and now seeks to purchase only unbundled transmission, and the other who previously used an alternative source of supply and seeks to purchase unbundled transmission from the utility) will pay substantially different rates for the same service. The error in this argument is that the two customers in the example are not "similarly-situated" precisely because one of them was a former bundled wholesale requirements customer of the utility for whom the utility may have incurred costs to meet reasonably expected customer demand, whereas the other was never a generation customer of the utility and thus appropriately bears no cost responsibility for stranded generation costs incurred by that utility. Indeed, this example illustrates precisely the reason underlying the Commission's stranded cost mechanism. If a utility had previously served a customer as a seller of generation as well as a transmitter, it is allowed an opportunity to show that it incurred costs based on a reasonable expectation of continuing to serve the power needs of that customer beyond the contract term. Similarly, contrary to Central Illinois Light's claim, if different treatment of different customers were to occur, it would not be due to "accidents of circumstance"—it would be the result of the conscious application by the Commission of its decision to give a utility the opportunity to recover stranded costs from a wholesale requirements customer if the utility can demonstrate that it incurred costs to provide service to the customer based on a reasonable expectation that it would continue to serve the customer after the contract term.

In response to the claims of those entities that challenge the factual record for allowing wholesale stranded cost recovery, we believe that the record in this proceeding clearly demonstrates the need to give utilities the opportunity to recover wholesale stranded costs. We have shown that the Rule's open access requirement will significantly alter historical relationships among traditional utilities and their customers. Indeed, that is one of its objectives. In the longer term, we seek to have all power supply arrangements priced by the competitive marketplace. However, utilities prudently incurred costs under a prior regulatory regime that created an expectation of an opportunity for recovery of those costs. Common sense indicates that a utility that historically supplied bundled generation and transmission services to a wholesale requirements customer and that reasonably expected to continue to serve the customer may have incurred costs to provide service to that customer that could be stranded if the customer uses open access transmission to reach a new generation supplier.[FN502] As we learned from our experience in restructuring of the natural gas industry, open access and unbundling did in fact exacerbate the take-or-pay problems in the gas industry because it gave customers more options. That is what we are doing in the electric industry as well. As a result, we have concluded that utilities should be permitted to seek recovery of stranded costs in certain limited and defined circumstances.

We disagree with those entities that argue that utilities have not provided sufficient data on the existence of wholesale stranded costs to justify the approach adopted by the Commission in Order No. 888. Presumably these entities would require us to calculate specific stranded cost estimates for every public utility before we could act to address this critical issue. However, where the Commission decides to act by means of a generic rule,[FN503] the Commission is not required to make individual findings on a utility-by-utility basis.[FN504] Moreover, the Rule does not say that all utilities with wholesale contract customers will be allowed to recover stranded costs, only that those utilities that have requirements contracts that were executed on or before July 11, 1994 that do not contain an exit fee or explicit stranded cost provision and that can meet the required evidentiary showing would be allowed such recovery. On this basis, our decision to give utilities the opportunity to seek stranded cost recovery for certain wholesale requirements contracts is not dependent on a showing that any particular utility will actually be eligible to recover stranded costs as a result of the open access requirement.[FN505]

We also will reject SC Public Service Authority's request that the Commission deny market-based rate authority for all utilities seeking stranded cost recovery. SC Public Service Authority has failed to demonstrate that the ability to seek stranded cost recovery would, by definition, eliminate the potential for mitigation of any generation or transmission market power. If an entity believes that a utility seeking market-based rate authority does not satisfy the Commission's criteria for the grant of market-rate authority (e.g., because the utility has, or has failed to mitigate, market power in generation or transmission), that entity will have ample opportunity to present its case in the market-based rate proceeding.

American Forest & Paper's objection that utilities that voluntarily filed open access tariffs cannot utilize the stranded cost provisions and therefore that only utilities who were forced to offer open access transmission are being rewarded is misplaced. First, there is nothing in Order No. 888 that prohibits a utility that voluntarily filed an open access transmission tariff from seeking recovery of stranded costs if it can demonstrate a reasonable expectation of continuing to serve a particular wholesale customer beyond the term of its existing contract. Second, many of the "open access" tariffs accepted prior to Order No. 888, while an improvement upon the status quo of no access, did not contain the minimum terms and conditions of non-discriminatory service, including functional unbundling. Order No. 888 required utilities that tendered for filing open access tariffs prior to the issuance of the Rule (Group 1 public utilities) to make section 206 compliance filings that ***12380** contain the non-rate terms and conditions set forth in the Open Access Rule pro forma tariff. That tariff expressly includes provisions allowing a transmission provider to seek to recover stranded costs in accordance with the terms, conditions and procedures set forth in Order No. 888. Of the 101 public utilities that had some version of open access available prior to Order No. 888, all now have open access tariffs on file that contain provisions that expressly allow the transmission provider to seek to recover stranded costs as provided in Order No. 888.

We also will decline San Francisco's request that the Commission include "exercise of pre-existing contract rights for transmission and designation of wholesale loads" or similar language as an example of a situation for which stranded costs may not be sought.[FN506] We are not prepared to make individual factual determinations in the context of this Rule.[FN507] As specific requests for stranded cost recovery are presented to the Commission, they will be addressed based on the facts presented and the merits of the particular request.

Rehearing Requests Seeking Broader Stranded Cost Recovery

In sharp contrast to the entities seeking rehearing of the Commission's decision to allow stranded cost recovery, other entities ask the Commission to expand the scope of the stranded cost recovery allowed by Order No. 888. Various entities ask that the scope of stranded cost recovery be expanded to include situations in which the departing customer does not take unbundled transmission from the former supplier and in which previously existing municipal utilities annex additional territory or otherwise expand.[FN508] These entities disagree with the Commission's analysis in Order No. 888 that the opportunity to seek recovery should be precluded in situations in which the departing wholesale customer ceases to purchase power from the utility but does not use the utility's transmission system to reach another supplier. The Commission excluded these situations because the costs would not be stranded as a result of the Commission's open access transmission requirement, but rather as a result of the exercise of a preexisting competitive option. The entities argue on rehearing that such costs are attributable to the Commission's efforts to restructure the wholesale power market. Several argue that there is no good policy reason for addressing stranded costs only where linked directly to the Open Access Rule or section 211 orders because a variety of federal actions, not just the Open Access Rule and section 211 orders, have created a competitive wholesale power market and the specter of stranded costs caused by customers departing their traditional utility. They contend that, but for the Commission's creation of a vibrant power market, EPAct, and other pre-Order No. 888 efforts by the Commission to expand transmission access, the preexisting options would not have been (and historically were not) exercised.

Puget argues that even when a departing customer can import its new power supply without using its former supplier's transmission system, it frequently will be the case that the power supply would not be available to the customer if open access transmission rules were not in place to permit that power to move from distant generators over intervening utilities' transmission facilities.[FN509]

EEI expresses concern that strict application of the "but for open access" test would create new incentives to evade stranded cost recovery.[FN510] According to EEI, the Rule would deny recovery for costs stranded pursuant to a voluntarily negotiated transmission service agreement, but would permit recovery if such agreement were ordered pursuant to FPA section 211. In this manner, EEI contends that the Rule will discourage parties from settling transmission disputes. It says that any transmission agreement negotiated under "the threat" of section 211 should be entitled to stranded cost recovery if providing service results in the stranding of legitimate and prudent costs.

PSE&G and Carolina P&L express concern that denying stranded cost recovery where the departing customer does not use the former supplier's transmission system will create an artificial incentive to build "contract path" lines designed to thwart stranded cost recovery. They maintain that the existence of alternative transmission paths should not be a bar to stranded cost recovery where the departing customer avails itself of the Commission's Mobile-Sierra finding permitting customers to challenge the terms of their contracts under the just and reasonable standard. They assert that, notwithstanding the availability of alternative transmission, the only way that the customer could have availed itself of the Mobile-Sierra finding was as a result of the Commission's Open Access Rule.

Several entities contend that the FPA's requirement of just and reasonable rates and the Fifth Amendment's requirement to avoid confiscation require the Commission to address stranded costs that result when a departing customer does not use the former supplier's transmission system or that result from municipal annexation.[FN511] According to Puget, the ultimate Constitutional test will be whether Order No. 888 will afford a fair overall return on all prudent utility investments under the Constitutional standards set forth by the Supreme Court.[FN512] Coalition for Economic Competition submits that, as was the case in the context of the unbundling of natural gas pipelines, the Commission cannot ignore stranded costs resulting from the unbundling of electric services and should acknowledge its Constitutional obligations to address the recovery of all stranded costs, including those that result from municipal expansion and those that result when a ***12381** customer does not obtain transmission services from its former supplier.

SC Public Service Authority also asks the Commission to allow the recovery of stranded costs that result from the loss of indirect customers (e.g., customers of wholesale requirements customers). It argues that if such indirect customers can get access to a new source of power through open access tariffs, the requirements of the utility's direct customer will decrease, and the supplying utility will suffer stranded costs. SC Public Service Authority states that because of the nexus between open access and the departure of the indirect customer, utilities that suffer stranded costs in the event of the loss of an indirect customer should have an opportunity to recover those costs under the reasonable expectation standard.

A number of entities also ask the Commission to find that open access transmission and stranded cost recovery are necessary to accomplish the remedy ordered by the Commission and thus are not severable.[FN513] To this end, they submit that if the Commission's ability to provide for stranded cost recovery is reduced or substantially modified, public utilities should be able to withdraw filed tariffs or to file amended tariffs. It is their position that deletion or substantial change of the open access or stranded cost provisions by the Commission or by a court would vitiate the basis on which the Commission premised the Rule.

In an effort to ensure that stranded cost recovery procedures do not become a vehicle for lengthy and expensive litigation over whether there is a sufficient nexus to open access, several entities ask the Commission to place on the departing generation customers the burden to demonstrate the absence of a nexus between their actions and the availability of open access transmission under the Rule in those cases where: (i) the contract has no term or termination provision; (ii) the Commission issues an order under section 206 reducing the term of the contract; or (iii) there is legitimate municipalization.[FN514]

Commission Conclusion

We will deny the requests for rehearing that ask us to expand the scope of stranded cost recovery to include situations in which the departing customer does not take unbundled transmission from its former supplier but instead obtains transmission from another utility or obtains power from a third party supplier who is located in the customer's service territory and thus requires no transmission from the former supplier.[FN515] As the Commission stated in Order No. 888, the premise of the Rule is that where the former requirements supplier had a reasonable expectation of serving beyond the contract term and the customer uses the open access transmission tariff of its former requirements supplier to obtain power from a new generation supplier, the customer must pay the costs that were incurred on its behalf under the prior regulatory regime. The Rule is not intended, however, to apply to the recovery of costs associated with the normal risks of competition, such as self-generation, cogeneration, or loss of load, that do not arise from the new, accelerated availability of non-discriminatory open access transmission. If a customer leaves its utility supplier by exercising options that could have been undertaken prior to mandatory transmission under Order No. 888 or the Energy Policy Act, or that do not rely on access to the former seller's transmission (such as access to another power supplier through another utility's transmission system or self-generation), there is no direct nexus to Commission-mandated transmission access.

For example, if a customer is able to obtain power from a new supplier by using the transmission system of another utility, it is likely that the customer could have made these arrangements in the absence of the new open access rules. The new transmission provider would have had little incentive to deny transmission services to the customer in order to protect another utility's existing power supply arrangement, since it was not the customer's power supplier in the first place. As Order No. 888 suggested, it is likely that the neighboring utility would have a positive incentive to provide the transmission service in order to increase its transmission revenues, and that this incentive is unchanged by open access transmission.[FN516]

Although EEI and others argue that EPAct and the Commission's pre-Order No. 888 efforts to expand transmission access have facilitated the exercise of pre-existing competitive options, the fact remains that such options historically were available before open access. For this reason, we conclude that costs incurred as a result of the exercise of pre-existing competitive options do not fall within the scope of Order No. 888.

A number of entities argue that, even where the departing customer obtains access to another power supplier through the transmission system of another utility (i.e., not that of its former supplier), the power supply would not have been available to the customer if open access transmission rules were not in place to permit that power to move from distant generators over intervening utilities' transmission facilities. Some argue that there is no good policy reason for addressing stranded costs only where linked directly to the Open Access Rule (or to a section 211 order) because a variety of federal actions have created a competitive wholesale power market and the specter of stranded costs caused by customers departing their traditional utility. While these arguments may have superficial appeal, the effective result would be to provide for recovery of stranded costs from departing customers under the Rule no matter how tenuous the nexus to Commission-mandated transmission access. The Commission has to exercise reasonable judgment and reasonable line drawing regarding the link between its actions in this Rule and the decision to allow an opportunity for extra-contractual stranded cost recovery from the departing customer. The Commission believes that requiring a direct nexus between Commission-mandated transmission access (namely, requiring that the departing customer obtain access to another power supplier through the use of its former supplier's Commission-required tariff—i.e., an open access tariff or a tariff ordered pursuant to section 211) and the special stranded cost recovery procedures of this Rule is the most reasoned and supportable approach because it establishes a clear link between availability of the transmission tariff ***12382** and the decision of the customer to seek an alternative supplier.

With regard to potential stranded costs associated with situations that could have occurred prior to the Open Access Rule and prior to the Energy Policy Act (such as self-generation), under traditional ratemaking such costs (albeit not previously labeled as potential "stranded" costs) would in most cases be reallocated in the next rate case to remaining customers. The fact that this Rule does not permit a utility to seek recovery of these types of costs from the departing customer does not mean that the Commission may not, in appropriate circumstances, permit their recovery through traditional ratemaking means. However, many factors will influence cost recovery in the future, including whether the utility is selling at cost-based or market-based rates and the transitional period to more competitive bulk power markets. The Commission will address these matters on a case-by-case basis.

We do not agree with those commenters who contend that the Commission's failure in Order No. 888 to allow for the recovery of costs incurred by a utility when a departing customer does not use the former supplier's transmission system to reach a new supplier would be confiscatory in violation of the Constitution. As the Supreme Court explained in Duquesne, "[t]he guiding principle has been that the Constitution protects utilities from being limited to a charge for their property serving the public which is so 'unjust' as to be confiscatory."[FN517] However, Order No. 888 addresses only the recovery of legitimate, prudent and verifiable costs that are stranded if a former wholesale requirements customer or a former retail customer uses a Commission-mandated transmission tariff to reach a new supplier. As discussed above, Order No. 888 does not by its terms bar the recovery of costs that do not result from the use of Commission-required transmission access (i.e., costs that result when a departing customer does not use the former supplying utility's open access tariff). Utilities may, as before, seek recovery of such non-open access-related costs on a case-by-case basis in individual rate proceedings. The Commission will not prejudge those issues here. As a result, the argument that the Commission's treatment of stranded costs in Order No. 888 (i.e., its failure to treat certain costs as costs for which recovery may be sought under the Rule) will result in rates that will be so unjust as to be confiscatory is misplaced.

We deny SC Public Service Authority's request that the Commission allow a utility to seek recovery of stranded costs that result from the loss of indirect customers (i.e., the loss of the utility's customer's customers). The Commission does not believe it is appropriate or feasible to allow a public utility (or a transmitting utility under section 211 of the FPA) to seek recovery of stranded costs from an indirect customer (i.e., a customer of a wholesale requirements customer of the utility). The reasonable expectation analysis would apply only to the direct wholesale customer of the utility, not to the indirect customer. A utility may seek to recover stranded costs from a direct wholesale customer (subject to the requirements of the Rule), but it is up to the direct wholesale customer, through its contracts with its customers or through the appropriate regulatory authority, to seek to recover stranded costs from its customers.

We also deny PSE&G's and Carolina P&L's request that a utility be allowed to seek stranded cost recovery in cases where the departing customer uses the Commission's Mobile-Sierra finding to get out of the contract under the just and reasonable standard and uses alternative suppliers and alternative transmission.[FN518] We disagree with their argument that the only way that the customer could have availed itself of a Mobile-Sierra finding was as a result of the Commission's open access rules and thus the necessary nexus is met. A customer to a Mobile-Sierra contract always has the option of instituting a proceeding under section 206 of the FPA and making a showing of why, under Mobile-Sierra, it is in the public interest to modify the contract.

We will not, at this time, make any determination whether or not the requirements of open access transmission and stranded cost recovery are severable. As we indicated in Order No. 888, we issued the Stranded Cost Final Rule simultaneously with the Open Access Rule because we believe that the recovery of legitimate, prudent and verifiable stranded costs is critical to the successful transition of the electric industry to a competitive, open access environment.[FN519] We believe that our decision to allow stranded cost recovery will be upheld by the courts. Moreover, as we discuss in Section IV.A.1 above, it would be premature to consider at this time what the Commission would do if one or more of the provisions of the Rule are not upheld. Circumstances at the time of any court order would dictate how we should proceed and we would consider all such circumstances, and the entirety of our policy decisions, before determining how to respond to a court decision.

Further, we decline to place on departing generation customers the burden of demonstrating that no nexus exists between their actions and the availability of open access transmission under the Rule in cases involving no term or termination provision, an order under section 206 reducing the term of the contract, or municipalization. The proponents of such a proposal, Carolina

P&L and PSE&G, attempt to justify it as a means to ensure that stranded cost recovery procedures do not become a vehicle for lengthy and expensive litigation over whether there is a sufficient nexus to open access in the three identified situations. However, Order No. 888 places the burden on the utility seeking stranded cost recovery to demonstrate that the costs for which it seeks recovery fall within the scope of the Rule and that it had a reasonable expectation of continuing service. In this regard, the Rule tracks the requirement of sections 205 and 206 of the FPA that a public utility demonstrate the justness and reasonableness of its proposed rates. Carolina P&L and PSE&G fail to explain why it would be appropriate for customers (as opposed to the utilities seeking recovery) in the three identified situations to bear the initial burden of demonstrating why costs should not be recovered from them under the Rule.[FN520] As a result, we reject their proposal.[FN521]

Rehearing Requests—Stranded Cost Recovery By Transmitting Utilities That Are Not Public Utilities

A number of entities contend that the Commission's decision to limit stranded cost recovery for transmitting utilities that are not public utilities to section ***12383** 211 proceedings is inconsistent with its decision to impose the reciprocity requirement on those utilities, violative of the principle of comparability, and unduly discriminatory and anticompetitive.[FN522] NRECA submits that if the Commission has the statutory authority to require non-public utilities to render transmission service outside of a section 211 proceeding through the reciprocity, RTG and power pool provisions of the Rule, then it must exercise that authority to ensure stranded cost recovery by such non-public utilities. Noting that the Rule does not address how a non-public utility that chooses voluntarily to provide an open access tariff can recover its stranded costs, SC Public Service Authority asks the Commission to confirm on rehearing that non-jurisdictional utilities can include a provision for recovery of stranded costs in their tariffs provided pursuant to the Final Rule.

Commission Conclusion

The Commission's jurisdiction over the recovery of stranded costs by non-public utilities, and thus our ability to permit an opportunity for recovery of such costs, is limited by statute. While we have the statutory authority to ensure that non-public utilities have the opportunity to seek recovery of stranded costs in proceedings under sections 211 and 212 of the FPA,[FN523] we do not have such authority under sections 205 and 206 of the FPA. However, we clarify that nothing in the Final Rule was intended to preclude non-public utilities from including stranded cost provisions in voluntary reciprocity tariffs or from otherwise recovering stranded costs under applicable law. We discuss these matters in detail below.

As we stated in Order No. 888 in response to commenters' objections that the Rule would give public utilities a greater opportunity than other transmitting utilities to recover stranded costs, our jurisdiction over transmitting utilities that are not also public utilities is limited. If the selling utility is a transmitting utility that is not a public utility, its power sales contracts are not subject to this Commission's jurisdiction under sections 205 and 206 of the FPA. Thus, we can provide such a transmitting utility an opportunity to recover stranded costs only through Commission-jurisdictional transmission rates fixed under sections 211 and 212 of the FPA.[FN524]

The open access tariff reciprocity provision, which applies to all open access customers that own, operate, or control transmission facilities or are affiliates of entities that own, operate or control such facilities, and that do not obtain a waiver of the provision, does not create jurisdiction for the Commission to fix the rates for these utilities. Contrary to the suggestions of some, the tariff reciprocity provision is not based on any statutory authority of the Commission to require non-public utilities to render transmission service outside of a section 211 proceeding. As we make clear in Order No. 888, we do not have authority under sections 205 and 206 of the FPA to require non-public utilities to file tariffs (or rate schedules for that matter) with the Commission.[FN525] In permitting a public utility to deny transmission service to any person that requests service under an open access tariff unless that person provides reciprocal non-discriminatory transmission services to the transmission provider, we are not acting under any statutory authority to require non-public utilities to provide transmission access. Rather, out of fairness, we are conditioning the use of open access services by all customers, including non-public utilities, on an agreement to offer comparable transmission services in return to the public utility transmission provider.[FN526]

We clarify that a non-public utility that chooses voluntarily to offer an open access tariff for purposes of demonstrating that it meets the reciprocity provision can include a stranded cost provision in its tariff. However, adjudication of any stranded cost claims under that tariff is not subject to the Commission's jurisdiction.[FN527] With the exception of our section 210 interconnection and sections 211-212 transmission rate jurisdiction, we do not have jurisdiction over the rates of non-public utilities. If a non-public utility wishes to recover stranded costs pursuant to a tariff or otherwise, it can seek to do so subject to the review of the appropriate regulatory authority.[FN528]

Rehearing Requests—Stranded Cost Recovery for Transmission Dependent Utilities

NRECA and TDU Systems challenge the Commission's decision not to guarantee a transmission dependent utility that is not a public utility stranded cost recovery when the transmission dependent utility's customers leave its system by using the open access tariff of another utility. They submit that the ability of transmission dependent utilities to compete with public utility transmission providers in an open access environment would be severely affected by their inability to recover stranded costs on a basis comparable to those transmission providers. They argue that the open access provisions of Order No. 888 will result in the stranding of costs incurred by non-transmission owning, non-public utilities to serve customers that depart to other suppliers. They contend that these customers are already located in close proximity to, and interconnected to, public utilities; thus it is likely that they would use the open access tariffs of these public utilities to obtain their new power supplies. NRECA and TDU Systems argue that this situation should meet the "but for open access" nexus. On this basis, they assert that Order No. 888 is no less the proximate cause of the departure of customers of transmission dependent utilities than it is of the departure of public utility transmission owners' customers. They object that the Commission takes no account of the anticompetitive effects of disregarding costs stranded on transmission dependent utilities' systems as a result of open access.

Dairyland Coop asks the Commission to recognize a generation and transmission (G&T) cooperative and its member distribution cooperatives as a single economic unit for purposes of stranded cost recovery (such that conversion of a distribution ***12384** cooperative's retail customer to a wholesale customer may result in stranded costs for the G&T cooperative). It objects that the Commission implicitly rejected comments to this effect without discussion in Order No. 888.

Commission Conclusion

We deny the requests for rehearing of our decision not to permit transmission dependent utilities and electric cooperatives to seek stranded cost recovery unless they are public utilities or transmitting utilities that would otherwise qualify under the Rule. With regard to transmission dependent utilities, as we indicated in Order No. 888, the limited opportunity for stranded cost recovery contained in the Rule would not likely apply in the case of transmission dependent utilities, who own little or no transmission and the majority of whom would not be public utilities or transmitting utilities subject to the Commission's jurisdiction.[FN529] The opportunity for extra-contractual wholesale stranded cost recovery is allowed only where the departing customers use open access (or section 211 access) on the transmission systems of their former generation suppliers and only for a discrete set of requirements contracts executed on or before July 11, 1994 that do not contain explicit stranded cost provisions (involving the bundled provision of generation and transmission) and retail-turned-wholesale situations for which the utility can demonstrate that it had a reasonable expectation of continuing service. Even though it may be the case that transmission dependent utilities lose generation customers that are able to use open access tariffs of other utilities to reach new suppliers, there was nothing to keep these other utilities from offering such transmission service before Order No. 888. These other utilities had no economic incentive to deny such service before Order No. 888. Thus, in the scenario posited in the rehearings, the transmission dependent utilities do not meet the fundamental premise of the Rule: that a utility that historically has supplied bundled generation and transmission services to a wholesale requirements customer and incurred costs to meet reasonably expected customer demand should have an opportunity to recover legitimate, prudent and verifiable costs that may be stranded because open access use of the utility's transmission system enables a generation customer to shop for power.[FN530]

However, this is not to say that a transmission dependent utility that is not a public utility, or other non-public utility entities (such as RUS-financed cooperatives), cannot seek recovery of the cost of any resulting uneconomic assets through their contracts with their customers or through the appropriate regulatory authority. The Commission has no objection to these entities being able to seek such cost recovery through the appropriate regulatory channels. However, because the Commission does not have jurisdiction over these entities (other than through sections 211 and 212 in the case of non-public utility transmitting utilities), it does not have authority to allow them to recover these costs.[FN531]

We also deny Dairyland Coop's request that the Commission recognize a G&T cooperative and its member distribution cooperatives as a single economic unit for purposes of stranded cost recovery. If a cooperative obtains its financing through RUS, it is not a public utility subject to our jurisdiction under sections 205 and 206 of the FPA. Although the Commission has no objection to these G&T cooperatives being able to seek cost recovery (including recovery of costs on behalf of their distribution cooperatives) through the appropriate regulatory channels, this Commission does not have authority to allow them to seek recovery of stranded costs unless access is obtained through a section 211 order.[FN532]

In the case of a G&T cooperative that is a public utility (of which there are just a handful at the present time), such a cooperative would have to have a jurisdictional wholesale requirements contract with its distribution cooperative in order to be able to seek recovery of stranded costs under the Rule. In the case of a jurisdictional G&T cooperative, the request that the G&T be treated as a single economic unit with the distribution cooperative (such that departure of a distribution cooperative's retail customer would be treated as resulting in stranded costs for the G&T cooperative for which the G&T could seek recovery) is, in effect, a request for recovery of stranded costs from an indirect customer. As we discuss above, the Commission does not believe it is appropriate or feasible to allow a public utility (or a transmitting utility under section 211 of the FPA) to seek recovery of stranded costs from an indirect customer (i.e., a customer of a wholesale requirements customer of the utility) under this Rule. The reasonable expectation analysis would apply only to the direct wholesale customer of the utility, not to the indirect customer. It is up to the direct wholesale customer of the utility, through its contracts with its customers or through the appropriate regulatory authority, to seek to recover such costs from its customers.

Commenters have provided no basis for making an exception in the case of cooperatives. Moreover, to treat a G&T cooperative and its member distribution cooperatives as a single economic unit for stranded cost purposes would be inconsistent with the Commission's decision not to treat cooperatives as a single unit for purposes of Order No. 888's reciprocity provision.

In Order No. 888, in response to arguments raised by cooperatives, the Commission agreed to limit the reciprocity requirement to corporate affiliates. In other words, if a G&T cooperative seeks open access transmission service from the transmission provider, only the G&T cooperative (not its member distribution cooperatives) would be required to offer transmission service. If a member distribution cooperative itself receives transmission service from the transmission provider, then it (but not its G&T cooperative) must offer reciprocal transmission service over its interstate transmission facilities, if any.[FN533] Dairyland has provided no basis to support treating cooperatives differently for stranded cost purposes and reciprocity purposes. We accordingly will deny Dairyland's request for rehearing on this issue.

Rehearing Requests Opposing Limitation of Recovery to Wholesale Requirements Customers

PA Munis argues that it is inequitable and anticompetitive for "wholesale requirements customers" but not other "wholesale customers" to have to pay stranded costs, repeating an argument that it made in its comments on the supplemental stranded cost NOPR. It says that there is no difference in the firm power provided by public utilities ***12385** to "wholesale requirements customers" and to "wholesale customers" and no difference in the generating facilities required and the costs of operation between the production of firm capacity and energy required for "wholesale requirements sales" and "wholesale sales." PA Munis submits that the total amount of wholesale requirements power purchased in the United States is less than two percent of the total amount of firm power sales. It argues that requiring only wholesale requirements customers to pay stranded costs would restrict the ability of such customers to switch suppliers while not similarly restricting large firm wholesale customers. It contends that wholesale firm requirements customers therefore will not have equal access under the Rule because of the increased transmission rates for stranded costs that would not be levied on other large wholesale firm customers. Pa Munis says this produces the same result found unlawful in the Maryland People's Counsel case[FN534]—equal access to all wholesale customers is virtually denied by the chilling effect of stranded costs borne only by wholesale requirements customers.

Commission Conclusion

In Order No. 888, the Commission fully addressed the concerns of PA Munis. We again address below the major distinctions between requirements and other customers and deny rehearing.

In Order No. 888, we explained that the historical and practical relationship between a utility and its wholesale requirements customers, including the expectation of continued service, justifies allowing public utilities the opportunity to seek to recover the stranded costs covered by this Rule from only those customers and not from non-requirements customers that contract separately for transmission services to deliver their purchased power or from wholesale customers that purchase non-requirements power. Requirements customers historically were long-term customers who by definition depended upon their local suppliers because they were captive customers. Utilities had no obligation to provide transmission service that would allow these customers to reach other suppliers, and there were no other transmission facilities in proximity to those of the supplying utility. And the service involved requirements power; that is, these customers were dependent upon the wholesale supplier for all or part of their power. Utilities thus assumed they would continue serving these customers and may have made significant investments based on that long-term expectation. These same assumptions cannot be made for short-term, non-firm transactions and other wholesale non-requirements firm transactions. Unlike requirements customers, these customers had other options. Thus, the supplying utility could not assume that these customers would remain on its system.

With regard to short-term transactions, utilities did not (and do not today) generally make investments for short-term economy-type transactions. Rather, such transactions were entered into only when the utility temporarily had available capacity or energy that could be provided to the buyer at a price higher than the seller's incremental cost and lower than the buyer's decremental cost. The utility was not obligated in any way—either explicitly or implicitly—to provide for the needs of coordination customers. Because coordination transactions were not the cause of stranded investment decisions, it would be inappropriate to allocate such costs to non-requirements customers.[FN535]

With regard to long-term, non-requirements firm transactions, such as unit power sales contracts, we note that there was no implied obligation to serve customers to these transactions as there was for requirements customers. Generating units were not built for the purpose of entering into these arrangements. Therefore, because utilities did not incur costs on behalf of non-requirements firm power sales customers, such customers have not caused costs to be stranded and should not be required to pay stranded cost charges. Accordingly, we reaffirm limiting the opportunity for stranded cost recovery to costs associated with wholesale requirements contracts.[FN536]

We recognize PA Munis' concern that if a utility meets the evidentiary requirements of the Rule and is allowed to recover stranded costs from wholesale requirements customers, such customers may see little or no savings in the short-term by switching power suppliers, since a stranded cost charge (in the form of either an exit fee or a surcharge on transmission) would be paid in addition to the power price paid a new supplier. However, as we discuss above and in Section IV.J.2 below, we believe that stranded costs are transition costs that must be addressed at an early stage if we are to fulfill our regulatory responsibilities in moving to competitive markets. Further, as we explain in Section IV.J.3 below, although spreading the costs to all transmission users of a utility's system (rather than imposing them directly on the departing wholesale requirements customer) might enable the customer to see earlier power cost savings than would result if stranded costs were directly assigned to the customer, we have concluded that this potential benefit to a broad-based approach is outweighed by a significant countervailing disadvantage—namely, the violation of the cost-causation principle of ratemaking. The Commission rejects a broad-based approach for the electric industry primarily because the potential power cost savings to the departing generation customer would be realized only by shifting costs that are directly attributable to the departing generation customer to the other users of the utility's transmission system.

Contrary to PA Munis's claim, we believe that the circumstances surrounding the opportunity to seek stranded cost recovery from wholesale requirements customers that is permitted in Order No. 888 are distinguishable from the issues that were before the court in the Maryland People's Counsel cases. Those cases involved challenges to Commission orders that permitted pipelines to transport gas at lowered prices to "non-captive consumers" (large industrial end users capable of switching to alternative fuels) without any obligation to provide the same service to "captive consumers" such as local distribution companies and their residential customers. In Maryland People's Counsel I, the court invalidated the Commission's authorization of a "special marketing program" under which a pipeline and its producer would agree to amend their high-priced gas purchase contract to permit the producer to sell the committed gas elsewhere at market prices and to credit the volume of such sales against the pipeline's high-priced purchase obligations. Eligibility to purchase the ***12386** cheaper released gas was limited to industrial users. The court found that the Commission had failed to provide a reasonable basis for its decision to exclude "captive customers" from eligibility to purchase the cheaper released gas.[FN537] In Maryland People's Counsel II, the court invalidated the Commission's approval of blanket authority for interstate transportation of natural gas sold directly by producers to fuel-switchable end users. The court held that the Commission had failed to consider the anticompetitive effects of failing to require the pipelines to provide the same service to captive consumers on nondiscriminatory terms.[FN538]

In contrast to the Maryland People's Counsel cases, the Commission in Order No. 888 is not discounting services for one class of customers to the exclusion of another, nor is it ordering that public utilities provide transmission access to only a specified customer group. To the contrary, Order No. 888 requires all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce to provide open access transmission to any "eligible customer," with "eligible customer" defined broadly to include "any electric utility (including the Transmission Provider and any power marketer), Federal power marketing agency, or any person generating electric energy for sale for resale."[FN539] Among other things, Order No. 888 gives wholesale requirements customers that previously were captive customers of their public utility suppliers the opportunity at the expiration of their contracts to take unbundled transmission service from their former suppliers in order to reach new suppliers. At the same time, the Commission recognizes that the departure of a wholesale requirements customer in this circumstance may strand costs that the former supplying utility incurred based on a reasonable expectation that it would continue to serve the customer beyond the contract term. As a result, Order No. 888 gives the former supplying utility the opportunity to seek recovery of costs stranded by the wholesale requirements customer's departure.

In further contrast to the Maryland People's Counsel cases, the Commission addresses in this Order (above) PA Munis' claim that it is inequitable and anticompetitive that only wholesale requirements customers and not other wholesale customers are subject to the stranded cost provisions of Order No. 888. The Commission has explained in detail the rationale for its decision that public utilities should be allowed an opportunity to seek to recover the stranded costs covered by this Rule only from wholesale requirements customers. The Commission has also addressed in Section IV.J.2 below the concerns expressed by some as to the potential anticompetitive effect of stranded cost charges.

Rehearing Request—ERCOT

The TX Com[FN540] asks the Commission to clarify that ERCOT utilities may not use a section 211 proceeding as a vehicle to obtain wholesale or retail stranded cost recovery.[FN541] It notes that based on the definitions in section 35.26 of "wholesale stranded cost"[FN542] and "wholesale transmission service,"[FN543] the Rule applies only to interstate service and does not apply to the intrastate service provided by the utilities within ERCOT, yet the Commission suggests that it might permit a utility in ERCOT to recover stranded costs in a section 211 proceeding. Even if the Commission concludes that it has the authority to resolve stranded cost issues for ERCOT utilities, TX Com asks the Commission to establish a preference for resolution of transmission and stranded cost issues in ERCOT by TX Com. It suggests that uncertainty and gaming as to the choice of a forum could be avoided by executing a Memorandum of Understanding between TX Com and the Commission that would require interested persons to submit disputes to TX Com. Further, to the extent that the new ERCOT transmission access rules adopted by the TX Com may be deemed as the cause of stranded costs in ERCOT, TX Com asserts that it should be allowed to resolve issues related to such stranded costs.

Commission Conclusion

In City of College Station, Texas,[FN544] the Commission repeated its view, first articulated in 1979, that sections 211 and 212 of the FPA clearly give the Commission jurisdiction to order transmission services within ERCOT, subject to the special rate provision for ERCOT utilities in section 212(k).[FN545] The Commission indicated that if it issues a final order in that case setting rates for transmission services within ERCOT, it will comply with section 212(k) and give deference to the TX Com's ratemaking methodology insofar as practicable and consistent with section 212(a).

Our jurisdiction to order transmission services within ERCOT includes the authority to address costs that are stranded by a section 211 transmission order.[FN546] Consistent with the special rate provision in section 212(k), we clarify ***12387** that we will give deference to the TX Com's ratemaking methodology, including any provisions or procedures related to stranded cost recovery, insofar as it is practicable and consistent with section 212(a) and consistent with the principle of comparability set out in Order No. 888.

2. Cajun Electric Power Cooperative, Inc. v. FERC [FN547]

In Order No. 888, the Commission explained why it does not interpret the Cajun court decision as barring the recovery of stranded costs and why the record developed in this generic proceeding fully addresses the court's concerns regarding meaningful access to alternative suppliers.[FN548]

We also addressed the court's concern that the method of recovery in that case (a charge in the departing customer's transmission rate) might constitute an anticompetitive tying arrangement. We explained that the stranded cost recovery procedure we prescribe in the Open Access Rule is only a transitional mechanism that is intended to enable utilities to recover costs prudently incurred under a different regulatory regime. The purpose and effect of the stranded cost recovery mechanism that we approved in the Rule is to facilitate the transition to competitive wholesale power markets. We concluded that while stranded cost recovery may temporarily delay some of the benefits of competitive bulk power markets for some customers, such transition costs must be addressed at an early stage if we are to fulfill our regulatory responsibilities in moving to competitive markets.

In reaching these conclusions, the Commission applied the traditional regulatory concept of cost causation. We stated that it is not an illegal tying arrangement to hold a customer accountable for the cost consequence of leaving an incumbent supplier if, under our rules, the incumbent supplier must show a reasonable expectation of providing continuing service to that customer before it can recover stranded costs from the customer.

In addition, in response to the Cajun court and commenters in this proceeding as to the need to provide as much certainty as possible for departing customers concerning their potential stranded cost obligation, the Commission included a formula for calculating a departing customer's potential stranded cost obligation. We explained that the revenues lost formula is designed to provide certainty for departing customers and to create incentives for the parties to address stranded cost claims between themselves without resort to litigation.

Rehearing Requests Arguing That the Commission Has Not Resolved the Cajun Court's Concerns

Several entities submit that the Commission has not resolved the Cajun court's tying concerns. They argue that tying arrangements are still the essence of the stranded cost recovery method mandated by Order No. 888, and that a tying arrangement is a per se antitrust violation that is not subject to justification by reference to the reasons for the restraint or the expected ancillary benefits.[FN549] A number of these entities object that the Commission does not address the court's substantive concern that a stranded cost provision is the antithesis of competition.[FN550] Several object that the Commission brushes aside the acknowledged anticompetitive effects of the rule as being “transitional only,” suggesting that short-term anticompetitive impacts are acceptable as long as the Commission is doing something that will be good for customers in the long term.[FN551] They also contend that the anticompetitive effects would not be limited to a transitional period, or that the transitional period could last indefinitely, thereby diluting or even nullifying the benefits of competition for years to come.[FN552]

Several entities submit that the Commission erred in concluding that the stranded cost rules contained in Order No. 888 would allow customers “meaningful” access to alternative power suppliers.[FN553] Among other things, these entities contend that there is no showing in the Order that transmission providers will not continue to exercise monopoly power over their transmission systems and that competition in generation will not be stifled by the stranded cost recovery mechanism.

Some entities also object that the stranded cost procedures contained in Order No. 888 fail to provide certainty in the computation of recoverable stranded costs. They argue that the prospect of stranded cost liability and related litigation add costs of potential deal-killing magnitude to any power supply acquisition considered by a customer.[FN554]

APPA and ELCON challenge the Commission's description of Western Resources, Inc. v. FERC[FN555] as affirming the Commission's ability to allow stranded cost recovery. APPA argues that Western Resources does not justify the stranded cost provisions of Order No. 888 because it was a filed rate doctrine case, not a stranded cost case. APPA says that Western Resources involved no consideration of any allegation of anticompetitive conduct and no allegation that the utilities' proposal constituted an illegal tying arrangement.

Commission Conclusion

We will deny the requests for rehearing advanced on the basis of the Cajun case. We disagree with those entities that contend that the Commission has not resolved the Cajun court's tying concerns. As an initial matter, we note that the parties that have raised this issue on rehearing ignore the fact that while this Commission has a responsibility to consider the anticompetitive effects of regulated aspects of interstate utility operations,[FN556] it has other statutory and regulatory public interest considerations which it must balance in order to engage in reasoned decisionmaking. In this proceeding, we have carefully balanced our responsibilities to remedy undue discrimination and to consider anticompetitive effects, our goal to eliminate market power of utilities and anticompetitive effects in the long run, and the need to provide a transition to competitive markets that is fair, that maintains a stable electric utility industry, and that recognizes the obligations incurred in a past, non-competitive regulatory regime. As discussed below, we do not believe that the stranded cost proposal adopted in the Rule results in an illegal tying arrangement, as argued on rehearing. We believe we have given reasoned consideration to any potential transitory ***12388** anticompetitive effects of our stranded cost policy and that we have met the directives of the court in Cajun.

In considering the Cajun decision, it is important to note that the Cajun court assumes the presence of a competitive market in the electric utility industry, but such a competitive market does not now exist. Instead, the Commission is in the process of trying to bring about a competitive market and to manage the transition thereto.[FN557] When the Commission undertook a similar restructuring in the gas industry, the D.C. Circuit invalidated the Commission's efforts precisely because the Commission had failed to deal with the stranded cost problem in a satisfactory manner.[FN558]

As we indicated in Order No. 888, we do not believe it is an illegal tying arrangement to hold a customer accountable for the consequences of leaving an incumbent supplier if, before the incumbent supplier can recover legitimate, prudent and verifiable stranded costs from the departing customer, it must show that it incurred costs to provide service to the customer based on a reasonable expectation of continuing to serve the customer. Order No. 888 provides no guarantee of stranded cost recovery. Moreover, Order No. 888 provides the opportunity to recover stranded costs only for a discrete set of wholesale requirements contracts—those executed on or before July 11, 1994 that do not contain an exit fee or other explicit stranded cost provision —and for retail-turned-wholesale customers. Thus, it is not necessarily the case that customers will have to pay stranded costs when they leave their current suppliers. To the contrary, before a utility can recover stranded costs from a customer, the utility must overcome certain evidentiary hurdles (including a rebuttable presumption of no reasonable expectation of continuing service if the contract contains a notice of termination provision). Particularly given the narrowly tailored circumstances under which stranded cost recovery is permissible under the Rule, we do not view it as the antithesis of competition.

We dismiss as misplaced the claims that Order No. 888's stranded cost recovery mechanism is a tying arrangement that is a per se antitrust violation that cannot be justified by reference to the reasons for the restraint or the expected ancillary benefits. Any "tying" that might result from the Rule is by regulatory order, not through monopoly power, and is justified as a means to avoid unfair cost shifting and to achieve the pro-competitive benefits of the Rule. As we stated in Order No. 888, the purpose and effect of the stranded cost recovery mechanism that we approve are to facilitate the transition to competitive wholesale power markets, not to prevent a generation customer of a utility from being able to reach alternative suppliers through its former supplier's transmission.[FN559]

To be sure, imposing a stranded cost charge might, in the short run, make some customers indifferent to whether they stay with their current suppliers and avoid stranded costs, or go with new suppliers but pay stranded costs to the former suppliers.[FN560] There is no question that, without the stranded cost recovery mechanism, some customers would be far more likely to switch to lower-cost suppliers and enjoy sooner the benefits of a competitive power market. But, as detailed in Order No. 888, such an approach may result in higher costs for other customers. We thus have had to balance the potential for earlier benefits for some customers against other public interest considerations, most particularly the need to provide a fair mechanism by which utilities can recover the costs of past investments under traditional regulatory concepts of prudently incurred costs and cost causation. The result is not to deny competitive advantages, but only to delay their full realization for some customers.

In any event, we do not believe that the Commission-imposed mechanism of allowing the utility to recover stranded costs from the departing customer through its transmission rates falls within the category of an illegal tying arrangement under the antitrust laws. As the Supreme Court has defined it, "[a] tying arrangement is 'an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier.'"[FN561]

Here there is no "tying" of "products."[FN562] Instead, the Rule provides a mechanism for recovering costs associated with a prior contract. We have not adopted a rule under which a customer may purchase transmission from a utility only on the condition that the customer also purchases a different product, namely, power, from the utility.[FN563] To the contrary, the Commission, through the Order No. 888 open access transmission requirement, is attempting to provide the customer with the opportunity to obtain unbundled transmission from a former supplying utility as a means to reach a new generation supplier. Whatever else, the stranded costs are not charges for "products" and thus there is no "tying" in the conventional sense. At best, there is only a condition: in obtaining unbundled transmission, the customer must also pay appropriate costs stranded by its use of Commission-required transmission access.

Finally, it is not clear how often departing customers will be obligated to pay stranded costs. Stranded cost recovery is by no means guaranteed under the Rule, nor is it clear what portion of a utility's uneconomic investment will be recoverable as stranded costs. Even when a utility is able to meet the evidentiary standard and the Commission approves imposition of a stranded cost charge, the customer is free to pay off its obligation immediately. If it chooses to pay off the stranded cost obligation over time, that charge would not be imposed indefinitely on the customer. We have limited the scope of contracts and costs for which utilities may seek stranded cost recovery. This limitation—to certain contracts and demonstrated costs—in our judgment fairly allocates between utility and customer the ***12389** burdens and benefits of open access transmission.

Nor is it true that the Rule does not allow customers "meaningful" access to alternative power suppliers. The Final Rule pro forma tariff contains terms and conditions ensuring the provision of non-discriminatory transmission service. The requirements that a public utility take service under its own tariff for wholesale sales and purchases, adopt a non-discriminatory transmission information network, and separate power marketing and transmission functions further ensure non-discrimination and remove constraints to fair competition. The result is meaningful access to alternative suppliers that goes far beyond what was offered in the transmission tariff under review in Cajun.

Contrary to the claims of some, the Open Access Rule does not guarantee that a utility may sell its power at market-based rates. The open access compliance tariff required by Order No. 888 does mitigate transmission market power.[FN564] However, the Commission's Rule does not generically grant market-based rate authority to utilities that file compliance tariffs. Utilities must still demonstrate on a case-by-case basis that they not only have mitigated transmission market power but also do not have market power in generation[FN565] or other barriers to entry.

Notwithstanding the objections by some commenters that the stranded cost procedures of Order No. 888 fail to provide certainty in the computation of stranded cost charges, we believe that directly assigning stranded costs to departing generation customers using the revenues lost formula is the fairest and most efficient way to balance the competing interests of those involved. The alternatives that we considered (an up-front broad-based approach or an as-realized broad-based approach) have significant disadvantages and are extensively discussed in Order No. 888.[FN566] Following a careful evaluation of the alternatives, we concluded that a revenues lost formula to calculate a customer's stranded cost obligation is more reasonable and provides greater certainty than would other approaches, such as those that rely on broad-based surcharge schemes that impose costs that may never be incurred or those that result in widely fluctuating transmission rates.[FN567] As we stated in Order No. 888, while we recognize that some commenters oppose the revenues lost approach as imprecise, any ratemaking method that relies on estimates will be subject to forecasting error.[FN568] Nevertheless, we have gone to great lengths to provide specificity with respect to the calculation of the components of the formula.

In response to those commenters that argue that Order No. 888's stranded cost procedures will add costs of potential deal-killing magnitude to any power supply acquisition considered by a customer, we believe that, to the contrary, use of the formula will narrow the scope of disputes over the calculation of stranded costs, lend precision to the stranded cost amount it produces, and provide certainty to departing generation customers with respect to their stranded cost obligations.

APPA and ELCON object to the Commission's reference to Western Resources as a case affirming the Commission's ability to allow stranded cost recovery. Notwithstanding their efforts to distinguish Western Resources (for example, as a filed rate doctrine case, not a stranded cost case, and as a case involving no allegation of anticompetitive conduct), they have failed to make a convincing argument that our description of that case as "confirm[ing] the validity of Commission-imposed stranded cost recovery mechanisms in the transition to competitive markets"[FN569] is not accurate. The case depends upon the validity of the Commission's decision to allow the recovery of costs stranded in the transition of the natural gas industry to a competitive market and supports the Commission's ability to allow stranded cost recovery in general. The same court, in United Distribution Companies, has recently confirmed the Commission's ability to allow the recovery of costs stranded in the transition to competitive markets, limiting its concerns to issues about "how" stranded costs should be recovered and from whom.[FN570]

3. Responsibility for Wholesale Stranded Costs (Whether To Adopt Direct Assignment to Departing Customers)

In Order No. 888, the Commission concluded that direct assignment of stranded costs to the departing wholesale generation customer through either an exit fee[FN571] or a surcharge on transmission is the appropriate method for recovery of such costs. We concluded that the departing generation customer (and not the remaining generation or transmission customers or shareholders) should bear the legitimate and prudent obligations that the utility undertook on that customer's behalf. In reaching this decision, we carefully weighed the arguments supporting direct assignment of stranded costs against those supporting the broad-based approach of spreading stranded costs to all transmission users of a utility's system. After a detailed review of the advantages and disadvantages of each approach, we concluded that, on balance, direct assignment is the preferable approach for both legal and policy reasons.[FN572] Our primary considerations were that direct assignment is consistent with the well-established principle that the one who has caused a cost to be incurred should pay that cost and that it will result in a more accurate determination of a utility's stranded costs than would an up-front, broad-based transmission surcharge.

The Commission also acknowledged that the direct assignment approach adopted in Order No. 888 is different from the approach taken for the natural ***12390** gas industry. We explained why we believe that difference to be justified by pointing out a number of differences between the transition of the electric industry to an open transmission access, competitive industry and the transition of the natural gas industry to open access transportation service by interstate natural gas pipelines.[FN573] We also declined to require a utility seeking stranded cost recovery to shoulder a portion of its stranded costs on the basis that such a requirement would be a major deviation from the traditional principle that a utility should have a reasonable opportunity to recover its prudently incurred costs, and explained why we applied a different approach in the gas area.[FN574]

Rehearing Requests Opposing Full Recovery From Departing Customers

A number of entities submit that the Commission has not adequately explained its decision not to require some utility sharing of stranded costs when the utility can satisfy the reasonable expectation criteria. They object that the Commission did not meaningfully consider the arguments made by commenters concerning utility responsibility (such as poor management decisions) for stranded costs.[FN575]

ELCON argues that departing customers are not the sole cause of stranded costs. IL Industrials submits that the statement in the Rule that utility shareholders "'had no responsibility for causing the legitimate, prudent and verifiable costs to be incurred'" is untrue.[FN576] It argues that although utilities may have had a legal obligation to serve and meet projected demands, how the utility chose to meet those obligations was under the utility's control. IL Industrials asserts that shareholders should bear some of the risk associated with the decisions of their management that were less than optimal. At a minimum, IL Industrials argues that the Commission should consider on a case-by-case basis (when it determines whether a utility has incurred legitimate and verifiable stranded costs) whether some amount of stranded costs should be shared with shareholders.

NASUCA challenges the Commission's statement in Order No. 888 that requiring a utility to shoulder a portion of its stranded costs "would be a major deviation from the traditional principle that a utility should have a reasonable opportunity to recover its prudently incurred costs."[FN577] It contends that there is no constitutionally guaranteed right of recovery of all prudent investment.[FN578] NASUCA further asserts that full recovery of uneconomic investment is not the norm. It submits that the Commission has rejected utility demands for full recovery of cancelled electric generation facilities.[FN579]

San Francisco cites Market Street as support for the proposition that the risk of unmarketability should fall, in whole or in part, on utility shareholders who knew of competitive risks and who have been compensated for those risks through rates of return.

A number of parties object that the Commission, in declining to require some shareholder sharing of stranded costs, is allowing the electric utility industry to claim more generous recoveries under Order No. 888 than it allowed the gas industry, and that it has provided no adequate rationale for this difference in treatment.[FN580] San Francisco states that although the Rule attempts to distinguish shareholder sharing in the natural gas industry "as an extraordinary measure given the nature of the take-or-pay problem and the prevailing environment at that time,"[FN581] the Commission has not identified how the nature of the take-or-pay problem was any more "extraordinary" than the nature of stranded costs in electric restructuring, or explain its reference to "the prevailing environment at that time."

Occidental Chemical submits that the Commission's decision not to allocate a portion of stranded costs to utilities on cost causation grounds contradicts the Commission's actions in Order No. 636, in which it required interruptible and new shippers, as beneficiaries of open access, to share in the costs of the transition.[FN582] Central Illinois Light states that the Commission should allow partial recovery of stranded costs and thereby correct key differences in the Commission's responses to gas and electric transition costs.[FN583]

Occidental Chemical also objects that the Commission failed to address the merits of its suggestion that the Commission grant a utility a presumption of prudence in return for absorbing a percentage of its stranded costs.

ELCON, in a supplement to its rehearing request,[FN584] submits that the D.C. Circuit's remand in United Distribution Companies of the aspect of Order No. 636 that allocated 100 percent of gas supply realignment costs to customers and none to pipelines has implications for the Commission's decision in Order No. 888 to allocate 100 percent of stranded costs to departing customers without any shareholder sharing of the costs. ELCON suggests that although the D.C. Circuit indicated that a finding of threat to the financial viability of the pipeline sector might justify such allocation, there is no evidence in the record in the Order No. 888 proceeding, and the Commission has made no finding, that wholesale stranded cost recovery jeopardizes the financial viability of the utility sector. It ***12391** adds that, to the extent the Commission relies on strict cost causation principles in Order No. 888, it is not clear how departing wholesale customers who signed contracts in 1985 could have "caused" utilities to incur uneconomic assets such as expensive nuclear facilities that were planned and ordered in the 1970s.

Commission Conclusion

As we explained in Order No. 888, we decided not to require a utility meeting the requirements for stranded cost recovery to shoulder a portion of its stranded costs because such a requirement would be a major deviation from the traditional principle that a utility should have a reasonable opportunity to recover its prudently incurred costs.[FN585] Our decision (which allows assignment of legitimate, prudent and verifiable stranded costs to departing requirements generation customers, not to shareholders or other customers of the utility) also follows the cost causation principle that has been fundamental to our regulation since 1935.[FN586] It is important, in this regard, to distinguish between assuring recovery of all uneconomic costs (which Order No. 888 does not do) and providing an opportunity for recovery where the evidentiary requirements of the Rule are met.

Allowing full recovery of stranded costs under Order No. 888 is not equivalent to allowing 100 percent recovery of the costs of all uneconomic assets. A utility may have uneconomic assets for a variety of reasons, including a decline in load, customer shifts to natural gas, customer energy conservation, loss of a large industrial customer, customer self-generation, and a customer gaining transmission access through another utility's transmission system. The Rule does not provide for the recovery of the costs of such uneconomic assets.

Instead, the Rule defines a discrete set of uneconomic costs that are stranded by FPA section 211 or Order No. 888 transmission service (when a customer uses the former supplying utility's transmission system to reach a new supplier) for which utilities may seek recovery. However, even as to this set of costs the Rule does not guarantee 100 percent recovery. To be eligible to recover such costs, a utility must satisfy the reasonable expectation test set forth in Order No. 888. Even then, the utility will be eligible to recover only costs that are legitimate, prudent and verifiable.

In response to those entities that argue that departing customers are not the sole cause of stranded costs and that poor management decisions may be partly to blame, we reiterate that a determination that a utility has a reasonable expectation of continuing to serve a customer would not, in all circumstances, mean that costs incurred by the utility were prudent. As we said in Order No. 888, we cannot make a blanket assumption that all claimed stranded costs were prudently incurred. We explained that prudence of costs, depending upon the facts in a specific case, may include different things, such as prudence in operation and maintenance of a plant, and the utility's ongoing obligation to exercise prudence in retaining existing investments and power purchase contracts and in entering into new ones.[FN587] We clarified, however, that we do not intend to relitigate the prudence of costs previously recovered.

Thus, to the extent that costs have not been previously recovered by a utility, and depending upon the facts presented, a customer from whom a utility is seeking to recover stranded costs may be able to challenge the prudence of those costs. If such prudence challenge is successful, then the utility would not be entitled to recovery of the imprudently incurred costs, through stranded cost recovery or otherwise. We believe that this fully addresses the concerns of those entities that contend that departing customers should not be responsible for costs that result from poor management decisions or other actions by the utility.[FN588]

As we explained in Order No. 888, our decision not to require utilities to shoulder a portion of their stranded costs is based on the traditional principle that a utility should have a reasonable opportunity to recover its prudently incurred costs.[FN589] NASUCA's reliance on the Commission's cancelled plant policy to support its argument that full recovery of uneconomic investment is not the norm is misplaced. The Commission's cancelled plant policy, which allows a utility to recover 50 percent of its prudently-incurred investment in a cancelled or abandoned plant, relates only to plants that are cancelled or abandoned prior to entering commercial service and thus prior to becoming used and useful.[FN590] The Commission has taken a different approach in the case of electric generating plants that are prematurely shut down after having been in commercial operation for a number of years. In the latter instance (which more closely resembles the type of costs for which a utility might seek recovery under Order No. 888 than does the cancelled plant before operation scenario), the Commission has allowed 100 percent recovery of prudently-incurred unamortized investment.[FN591]

***12392** San Francisco's and NASUCA's reliance on Market Street is also distinguishable. That case involved an industry (street railway) that had been rendered economically obsolete by market forces. The electric industry today, in contrast, is clearly not obsolete. Moreover, the costs that Order No. 888 gives a utility an opportunity to recover even in the face of market forces would not become stranded but for statutory and regulatory changes.

A number of parties contend that the Commission has not provided an adequate rationale for its different treatment of shareholder sharing in the natural gas industry. ELCON also relies on the D.C. Circuit's remand in United Distribution Companies of Order No. 636's holding that pipelines could recover 100 percent of their gas supply realignment (GSR) costs. After further review of this matter in light of the Court's decision in United Distribution Companies, we reaffirm that, even though the Commission permitted pipelines to recover take-or-pay costs based on "cost spreading" and "value of service" principles, stranded electric utility costs should be recovered based on traditional cost causation principles. This is because, despite the fact that both sets of costs are incurred in connection with a transition to unbundled, open access service, there are also substantial differences between the circumstances surrounding the two industries' incurrence of their respective transition costs.

The pipelines' take-or-pay problems began before the Commission initiated open access transportation in Order No. 436. The severe gas shortages of the 1970s led to enactment of the Natural Gas Policy Act (NGPA), which initiated a phased decontrol of most new gas prices and established ceiling prices for controlled gas, including incentive prices for price-controlled new gas higher than the ceiling prices previously established by the Commission under the NGA.[FN592] To avoid future shortages, pipelines then entered into long-term take-or-pay contracts at the high prices made possible by the NGPA, and those high prices stimulated producers to greatly increase exploration and drilling.[FN593] When demand unexpectedly fell and supply increased, the pipelines found themselves contractually bound to take or pay for high-priced gas which they could not sell. Even before Order No. 436 issued in October 1985, pipeline take-or-pay exposure was approaching $10 billion.[FN594] In 1986, as pipelines were just beginning to implement open access transportation under Order No. 436 and before the August 1987 issuance of Order No. 500, the pipelines' outstanding unresolved take-or-pay liabilities peaked at $10.7 billion.[FN595]

The Commission and the industry had never previously faced a take-or-pay problem of this nature or magnitude. In earlier times, pipelines had made take-or-pay payments to particular producers, and the Commission had a policy of permitting such payments to be included in rate base and then recovered as a gas cost when the pipeline later took the gas under make-up provisions in the contract.[FN596] By 1983, however, the pipelines could not manage their take-or-pay problems, and stopped honoring the bulk of their take-or-pay liabilities.[FN597] They then sought settlements with the producers to reform or terminate the uneconomic take-or-pay contracts and to resolve outstanding take-or-pay liabilities. Because pipelines had never previously incurred significant take-or-pay settlement costs, the Commission had no policy concerning whether and how pipelines were to recover those costs. The Commission commenced establishing such a policy in an April 1985 policy statement,[FN598] just six months before Order No. 436. When Order No. 500 issued, few take-or-pay settlement costs had yet been included in pipelines' rates. However, since the pipelines' outstanding take-or-pay liabilities were in the neighborhood of $10 billion, it was clear that pipelines would incur massive costs in their settlements with producers.

In short, when the Commission first addressed the issue of how to allocate take-or-pay settlement costs in Order No. 500, it did so under the shadow of the pipelines' vast outstanding take-or-pay exposure. The essential problem, therefore, was to decide which customers' rates should be raised to reflect the billions of dollars of take-or-pay settlement costs that the pipelines were incurring, but that the pipelines had still not filed to recover. To have allocated those costs solely to any one segment of the industry would have imposed a crushing new burden on that segment. For example, if the Commission had allocated the take-or-pay settlement costs entirely to bundled sales customers who chose to convert to transportation-only service, those customers would have ended up far worse off than if they remained as bundled sales customers.

As a result of all these facts, the fundamental premise of Order No. 500 was, as the Court expressed it in KN Energy, that "the extraordinary nature of this problem requires the aid of the entire industry to solve it."[FN599] In order to accomplish this result, Order No. 500 established an equitable sharing mechanism for pipelines to use in recovering their take-or-pay settlement costs as an alternative to recovery through their commodity sales rates. Relying on "cost spreading" and "value of service" principles, the Commission permitted pipelines to allocate their take-or-pay settlement costs among all the pipelines' customers. The Commission also required the pipelines using the equitable sharing mechanism to absorb a portion of the costs in return for the ability to recover an equal portion through a fixed charge. Importantly, pipelines using the equitable sharing mechanism and agreeing to absorb a portion of the costs were given a presumption that their take-or-pay settlement costs were prudent. Those who did not choose to avail themselves of the sharing/absorption mechanism could still file for recovery of take-or-pay costs pursuant to the traditional ratemaking methodology. Because the pipelines' cash flow problems were so severe and they could not reasonably expect to recover their costs through their sales ***12393** rates, they readily availed themselves of the special mechanism, with its presumption of prudence, rather than the more protracted traditional ratemaking option.[FN600]

The Court in KN Energy upheld the Commission's use of cost spreading in connection with the allocation of take-or-pay costs among a pipeline's open access customers.[FN601] The Court held that "the ratemaking rationales of Order No. 500 can be reconciled with the NGA, given the unusual circumstances surrounding the take-or-pay problem, and the limited nature—both in time and scope—of the Commission's departure from the cost-causation principle."[FN602] The Court emphasized that "[w]e hold only—and quite narrowly—that in the context of Order No. 500 the Commission has not betrayed its obligations to the NGA or precedent by employing these ratemaking principles in its attempt to bring closure to the take-or-pay drama."[FN603]

The unusual circumstances that justified the departure from cost causation principles in Order Nos. 500/528 are not present in the electric industry. In Order No. 888's discussion of the Commission's decision not to order any generic abrogation of existing requirements and transmission contracts between electric utilities and their customers, we have already pointed out:

At the time the Commission addressed this situation in the natural gas industry, it was faced with shrinking natural gas markets, statutory escalations in natural gas prices under the Natural Gas Policy Act, and increased production of gas. In other words, there was a market failure in the industry. * * * In contrast, there is no such market failure in the electric industry.[FN[604]]

The electric utility costs potentially stranded by Order No. 888 are fixed costs arising from the utility's electric generation business, including, for example, depreciation expense associated with the utilities' own generation facilities and a return on the original cost of its investment in those facilities. They also include costs associated with mandatory QF purchase contracts. Unlike take-or-pay settlement costs, these costs are not an extraordinary expense that the Commission has never previously encountered. Rather, the stranded electric costs that are subject to the direct assignment provisions of Order No. 888 are ordinary costs that have always been, and are currently, included in the utility's rates for electric generation approved by the Commission. And there is no pre-existing industry-wide market failure. Thus, we are not confronted at the start of the electric open access program with a vast outstanding cost not currently reflected in the electric utilities' rates, as we were at the start of the natural gas open access program.

Therefore, unlike the situation with the natural gas industry, stranded electric utility costs can be allocated among customers based upon traditional cost causation principles without imposing inequitable and unreasonable burdens on particular customer classes. Direct assignment to departing requirements generation customers through the stranded cost recovery mechanism contained in the Rule is consistent with the traditional cost causation principle because it recognizes the link between the incurrence of stranded costs and the decision of a particular generation customer to use open access transmission on the utility's system to leave the utility's generation system and shop for power, and bases the utility's ability to recover stranded costs on its ability to demonstrate that it incurred costs with the reasonable expectation that the customer would remain on its generation system beyond the term of the contract. The stranded costs are measured as the difference between revenues the utility would have recovered from the customer and the market value of the utility's power.

In essence, therefore, all that the direct assignment provisions of Order No. 888 require is that certain customers (those whom a utility is able to demonstrate it reasonably expected to continue serving beyond the contract term) who convert to transmission-only service continue, for a period, to bear certain generation costs that they were previously bearing. This helps to minimize immediate cost shifts to the remaining generation customers, and is thus consistent with the Court's concerns in AGD about cost shifts due to open access transportation.[FN605] At the same time, it does not impose any crushing new burden on the converting generation customers, as would have happened if in the natural gas industry the Commission had allocated the take-or-pay settlement costs entirely to pipeline sales customers who converted to transportation-only service.

On the issue of utility absorption of stranded costs, as ELCON points out, the D.C. Circuit in United Distribution Companies remanded Order No. 636 to the Commission for further explanation as to why the Commission had exempted pipelines from sharing in Order No. 636 GSR costs in light of: (1) Its reliance on "cost spreading" and "value of service" principles in allocating GSR costs among the pipelines' customers, and (2) the absorption requirement in Order Nos. 500/528. As the Court explained:

If the Commission intends to assign GSR costs according to these 'cost spreading' and 'value of service' principles, it must do so consistently or explain the rationale for proceeding in another manner. We approved the invocation of those principles in KN Energy because FERC had concluded that the take-or-pay crisis could be resolved only by spreading costs throughout the 'entire industry' 968 F.2d at 1301 (emphasis added), and because we recognized that 'all segments of the industry' * * * will benefit, id. (emphasis added), from restructuring.[FN[606]]

For the reasons discussed above and in Order No. 888, we have chosen to use traditional cost causation principles both in allocating stranded electric costs to certain electric utility customers and in finding that the utilities should be given an opportunity for full recovery of certain legitimate, prudent, and verifiable stranded costs. Thus, Order No. 888 does not present the issue of whether the Commission inconsistently applied ratemaking principles to the recovery of stranded costs that was of concern to the court in United Distribution Companies when it remanded the analogous portion of Order No. 636.

Moreover, based on the facts summarized above, the Commission concludes that the rationale we used to support the Order Nos. 500/528 absorption requirement is not valid for electric utility costs stranded by Order No. 888. Order No. 528-A, where the Commission gave its fullest justification for that absorption requirement, did not rely on either the "cost spreading" or "value of service" rationales to support the absorption requirement.[FN607] Order Nos. 500/528 consistently recognized that the Commission must "provide a pipeline a reasonable opportunity to ***12394** recover its prudently incurred costs."[FN608] However, Order No. 528-A reasoned that, because the take-or-pay problem was caused more by general market conditions than by any regulatory action of the Commission, it was appropriate to require the pipelines to share in the losses arising from those market conditions as a condition to using the alternative recovery mechanism.[FN609]

In these circumstances, the Commission concludes that it would not be reasonable to require electric utilities to bear costs that, unlike the Order Nos. 500/528 take-or-pay costs, arise as the direct result of Congress' and the Commission's change in the regulatory regime through FPA section 211 and Order No. 888. This is particularly the case since the electric utilities' potential stranded costs relate to large capital expenditures or long-term contractual commitments (some mandated by federal law) to buy power made many years ago in reliance on the preexisting regulatory regime.

Moreover, in a separate order, the Commission is responding to the United Distribution Companies remand by reaffirming the policy established in Order No. 636 that pipelines should be permitted full recovery of their prudently incurred GSR costs. In that order, the Commission finds that the rationale Order No. 528-A used to support the Order Nos. 500/528 absorption requirement is inapplicable to GSR costs. The remand order explains that, in the face of extraordinary market conditions, Order Nos. 500/528 adopted extraordinary measures. However, as we are finding here with respect to stranded electric utility costs, the remand order holds that the extraordinary market circumstances that gave rise to the requirement for pipeline absorption of gas supply costs in Order Nos. 500/528 were not present at the time of Order No. 636. Even before the Commission initiated open access transportation in Order No. 436, the market was preventing pipelines from recovering costs incurred under their take-or-pay contracts. The Order Nos. 500/528 absorption requirement reflected the preexisting effect of the market, which would have required absorption even without open access transportation under Order No. 436. The remand order finds that, contrary to the situation when Order No. 436 issued, at the time of Order No. 636, pipelines were generally able to take gas under their few remaining high-priced take-or-pay contracts from the late 1970s and early 1980s and were no longer accumulating significant additional take-or-pay obligations. This was because the pipelines were still performing a significant sales service and had reformed most of their uneconomic take-or-pay contracts.[FN610]

The remand order accordingly holds that the Commission's regulatory actions in Order No. 636 have caused the pipelines to incur the GSR costs. This is particularly the case because Order No. 636 required the pipelines to unbundle their natural gas and transportation sales and forbade the pipelines from making sales unless they were made by a separate sales or marketing entity. Order No. 888 also requires generation or commodity sales to be unbundled from sales of transmission. In these circumstances, traditional ratemaking principles require the Commission to allow the pipelines an opportunity to recover the full amount of the expenses caused by its actions. Thus, the Commission's approach to Order No. 636 GSR costs is similar to its approach in Order No. 888 to stranded electric generation costs.

Rehearing Requests Citing Other Inconsistencies Between Commission Treatments of the Gas and Electric Industries

VT DPS and Valero submit that Order No. 888 does not satisfactorily distinguish the Commission's rejection of gas pipelines' attempts to impose exit fees on departing customers. They argue that the Commission opposed the imposition of such exit fees in the gas context as anticompetitive because it would force customers desiring to switch suppliers when their contracts expired to pay the supply costs of both the new and former suppliers.

VT DPS and Valero take issue with the Commission's attempt to distinguish a recent El Paso case[FN611] as a "post-restructuring" case under Order No. 636. They contend that the Commission consistently applied the same policy (rejection of gas pipeline attempts to impose exit fees) before restructuring under Order No. 636. They further claim that the Commission cannot articulate a plausible basis for permitting utilities with notice provisions to file for exit fees, having denied El Paso's proposal outright without giving it an opportunity to rebut the presumption.

VT DPS and Valero also state that the "stranded" costs for which the Commission allowed recovery under Order No. 636 were costs that would be rendered unrecoverable because the costs would not be incurred to provide transportation service and because there would be no wholesale load from which to recover the costs. They indicate that the Commission has held that such gas costs are stranded only if rendered unrecoverable as a direct result of the restructuring required under Order No. 636. They submit that when a utility loses wholesale load or a municipality establishes a new distribution system and the utility cannot resell the capacity left unused, the utility's costs are not necessarily "stranded"—i.e., rendered unrecoverable—any more than if the utility's load declines because of conservation, an economic downturn or an increase in self-generation. They argue that the Commission should limit utility stranded cost claims solely to those cases where the utility can demonstrate that its costs have been rendered unrecoverable as a direct result of the Rule.

Commission Conclusion

We explained in Order No. 888 why we disagree with the argument that the Commission cannot impose an exit fee to recover stranded costs because the Commission did not allow gas pipelines to do so. We noted that the Rule establishes procedures for providing a potential departing generation customer advance notice (before it leaves its existing supplier) of the stranded cost charge (whether it is to be paid as an exit fee or a transmission surcharge) that will be applied if the customer decides to buy power elsewhere and the Commission decides the utility has satisfied the stranded cost recovery criteria of the Rule, e.g., the reasonable expectation criterion. We indicated that in the natural gas context, in contrast, the Commission has prohibited ***12395** pipelines from developing and charging an "exit fee" after a customer had implemented its gas purchase decision, noting that otherwise, the customer would not know in advance the full cost consequences of its nomination decision.[FN612]

We continue to believe that the Commission's decisions concerning natural gas pipeline exit fees, relied on by VT DPS and Valero, are not inconsistent with Order No. 888's limited approval of exit fees for the recovery of certain stranded electric utility costs. VT DPS and Valero point first to two cases decided by the Commission in 1988 and 1989 involving Gas Inventory Charges (GICs) proposed by Transwestern Pipeline Company (Transwestern)[FN613] and El Paso Natural Gas Company (El Paso)[FN614] pursuant to our Order No. 500 policy statement. However, those cases are not relevant here, essentially because the exit fees at issue in those cases were not designed to recover costs arising from the transition to open access transportation, unlike the stranded electric utility costs at issue here.

In the Transwestern case cited by VT DPS and Valero, Transwestern included in its proposal to implement a GIC a request for permission to assess an exit fee. The exit fee would have been charged to its largest local distribution company customer if that customer initially chose to nominate purchases under the GIC but then subsequently reduced its nominations. The Commission found the proposed exit fee inconsistent with both (1) its policy that GIC customers know in advance the full cost consequences of their nomination decisions and (2) its objective that prices under the GIC be constrained by market forces.

However, this holding was not applicable to Transwestern's recovery of costs incurred as part of its transition to open access transportation, since the Commission did not intend the GIC as a vehicle for recovery of such transition costs. The GIC was intended solely as a forward-looking charge that would recover costs the pipeline would incur in the future under its reformed, market responsive gas supply contracts.[FN615] The Commission's intent was that, before implementing GICs, pipelines would negotiate settlements of their existing uneconomic take-or-pay contracts and file to recover the resulting settlement costs under the Order No. 500 equitable sharing mechanism.[FN616] Indeed, in the Transwestern order cited by VT DPS and Valero, the Commission suggested that Transwestern postpone implementation of its GIC until it had renegotiated its supply contracts and filed to recover the resulting costs under the Order No. 500 equitable sharing mechanism.[FN617]

That mechanism included a fixed take-or-pay charge analogous to the direct assignment provisions of Order No. 888. The Commission permitted pipelines to allocate to sales customers who converted from sales to transportation the same fixed take-or-pay charge that those customers would have been allocated had they not converted.[FN618] Moreover, in a later order involving Transwestern's recovery of take-or-pay settlement costs under its Order No. 500 equitable sharing mechanism, the Commission expressly held:

In appropriate circumstances, the Commission may approve exit fees for departing customers, either through a condition on the abandonment of the purchase obligation of customers subject to the Commission's jurisdiction or through tariff language giving appropriate notice of such a fee before the departure.[FN[619]]]

As discussed in the preceding section of this order, the direct assignment provisions of Order No. 888, in essence, require that certain electric generation customers who convert to transmission-only service continue, for a period, to bear certain generation costs that they were previously bearing. That requirement is similar to the Commission's requirement, in connection with its Order No. 500 program, that pipeline sales customers who convert to transportation-only service continue to pay the same Order No. 500 fixed take-or-pay charge as they would have paid had they not converted.

VT DPS and Valero also claim that permitting electric utilities to recover stranded generation costs through exit fees to customers converting to transmission-only service is inconsistent with our 1995 order in El Paso,[FN620] rejecting that pipeline's exit fee proposal. We see no inconsistency. El Paso proposed, several years after its restructuring pursuant to Order No. 636, to impose an exit fee on its firm transportation customers who terminated or reduced their firm transportation service. The fee was designed to require the departing firm transportation customer to continue to pay a portion of El Paso's fixed transmission costs for a period of time after the customer's departure. The fee bore no relationship to El Paso's pre-restructuring merchant function, since it was designed to recover El Paso's costs of performing open access transportation service after its restructuring.

In both Order No. 888 and this order, we are acting consistently with El Paso. Similar to our refusal in El Paso to permit a pipeline to impose an exit fee on customers departing its transportation system altogether (whether for all or a portion of their firm service), so also here we are refusing to permit electric utilities to recover stranded costs from customers who depart their transmission systems altogether. We believe that, in that situation, there is no direct nexus between the customer's departure (and the stranding of costs) and Commission-required transmission access, since the customer is not using its former supplier's open access tariff to reach an alternative power supplier.

Order No. 888 thus permits an exit fee only to electric generation customers who, although they stop purchasing power from the utility, become transmission-only customers of the former supplying utility.[FN621] By contrast, ***12396** El Paso proposed an exit fee to transmission customers terminating their transmission service. In short, the exit fee we have found acceptable in

Order No. 888 is related to the electric utility's pre-restructuring generation service, unlike El Paso's rejected exit fee, which bore no relationship to El Paso's pre-restructuring merchant service.[FN622]

Finally, VT DPS's and Valero's comments concerning the Commission's treatment of Order No. 636 "stranded costs" attempt to make distinctions that do not make a difference for purposes of the Commission's treatment of Order No. 888 stranded costs. We have explained above that the electric industry's transition to an open transmission access, competitive industry is different in a number of respects from the natural gas industry's transition to open access transportation service by interstate natural gas pipelines. We also have explained why a different approach to recovery of legitimate, prudent and verifiable stranded costs in the electric industry is justified. On this basis, the Commission's definition and treatment of "stranded" costs under Order No. 636 need not dictate our definition and treatment of stranded costs under Order No. 888. In any event, in response to VT DPS's and Valero's request that the Commission limit utility stranded cost claims solely to those cases where the utility can demonstrate that its costs have been rendered unrecoverable as a direct result of the Rule,[FN623] we note that Order No. 888 does require a causal nexus between the availability and use of Commission-required transmission access and the stranding of costs.

Rehearing Requests Opposing Recovery of Stranded Costs in Transmission Rates

VT DPS and Valero submit that although the Commission has not proposed to depart from cost-based ratemaking methodologies in establishing transmission rates, Order No. 888 contravenes cost causation principles by recovering generating costs in transmission rates.[FN624] They argue that although the court in KN Energy held that the Commission might depart from strict cost-causation principles to permit pipelines to recover gas supply costs from transportation customers in extraordinary circumstances, the "extraordinary circumstances" were that the pipelines had no remaining sales customers and thus were left with no vehicle for recovering gas supply costs. On this basis, the court approved a mechanism under which gas supply costs were spread over virtually all transmission users. They describe as incongruous the Commission's claim in Order No. 888 that permitting direct assignment of stranded power costs in a transmission rate is a cost-based approach.

VT DPS and Valero further argue that even if the Commission were inclined to justify stranded cost recovery from departing customers on non-cost grounds, the Commission cannot show that the circumstances justifying similar cost recovery from gas pipeline transportation customers exist at the wholesale level in the electric industry because: (1) unlike its approach to gas pipelines, the Commission has not proposed to allow existing wholesale electric customers to get out of their contracts early; (2) there is no industry-wide problem; wholesale sales account for only a small fraction of the total business of regulated electric utilities, while gas pipelines had virtually all wholesale sales; and (3) direct assignment of generating costs only to departing customers is the antithesis of the cost-spreading rationale that provided the justification for the limited departure from cost-causation principles permitted in KN Energy. They contend that, in any event, the Commission cannot spread costs broadly even if they are recovered from all transmission customers because the largest users are retail customers that would be exempt from wholesale stranded cost surcharges.

A number of other entities also oppose the recovery of stranded generation costs in transmission rates.[FN625] Some of them contend that section 212(a) of the FPA limits the transmitting utility to the recovery of transmission-related costs.[FN626] PA Munis contends that the plain language of section 212, as amended by EPAct, limits the rates that can be charged under a section 211 order to those "'which permit the recovery by such utility of all the costs incurred in connection with the transmission services and necessary associated services * * *'"[FN627] PA Munis contends that Congress would not have limited recovery to the costs incurred in connection with the transmission services and necessary associated services if it had intended to allow the transmission rates to include part of a utility's costs for unused generation facilities completely unrelated to the cost of the transmission facilities.[FN628] PA Munis asserts that the legislative history of EPAct supports its position that there is no authorization for the Commission to include unused generation costs as part of the transmission costs that are allocable to transmission under section 212.[FN629]

AR Com and MO/KS Coms argue that the FPA does not allow the Commission to include costs in a transmission rate that are not caused by the provision of transmission service.[FN630] MO/KS Coms contend that retail stranded costs are largely generation costs that were not caused by any request to use transmission service or by any actual transmission usage, and are not an opportunity cost of providing transmission service. Citing the language in section 212 of the FPA allowing the transmitting utility to recover "all costs incurred in connection with the transmission services and necessary associated services," AR Com contends that nowhere does the Energy Policy Act or any other relevant statute authorize the collection of retail, non-transmission costs through transmission rates.

Commission Conclusion

We disagree with VT DPS's and Valero's argument that Order No. 888 contravenes cost causation principles by recovering generating costs in transmission rates. As the court in United Distribution Companies stated: "'Cost causation' correlates costs with those customers for whom a service is rendered or a cost is incurred."[FN631] Whether stranded costs are recovered through a surcharge on the transmission rates of a departing generation customer, or through an exit fee, the point is that under Order No. 888 they are recovered from the customer that caused them to be incurred. The only distinction is the mechanism by which they are recovered from that customer.

The Commission is not aware of any prohibition on permitting recovery through a transmission rate of what has traditionally been recovered through the generation component of a rate, so long as the utility does not double recover and the customer does not pay more than the costs that it caused to be incurred.[FN632] Indeed, the Commission has been upheld in permitting opportunity costs (foregone economic savings) to be charged as a transmission rate when they are higher than a traditional embedded cost transmission rate.[FN633] There is no significant difference between an "opportunity cost" component of a transmission rate and a stranded cost charge imposed through transmission rates. Both concern the recovery of generation costs. To be sure, in the former case these generation costs are incurred by reason of using high cost generation instead of substituting lower cost generation, and in the latter case the costs are "incurred" by reason of the loss of a customer.[FN634] But, for purposes of cost recovery, these are distinctions without a difference. In both situations, the transmission rate is used to recover something other than the capital, operating, and maintenance costs of facilities used to provide the transmission service at issue. If the Commission were without authority to provide for cost recovery of these other types of costs in transmission rates, the court would not have affirmed the volumetric surcharge on transportation in KN Energy, nor would it have affirmed the opportunity cost charge in Penelec.

As we note above, we are not proposing a departure from strict cost-causation principles such as that allowed in KN Energy, where the pipeline was allowed to recover 50 percent of its take-or-pay settlement costs through a volumetric surcharge on all transportation customers, including those that had never purchased gas from the pipeline.[FN635] Because we disagree with VT DPS's and Valero's position that recovery of stranded costs through a surcharge on transmission constitutes recovery on non-cost grounds,[FN636] we will reject their requests for rehearing on this issue.[FN637]

We also reject the argument that section 212 of the FPA prohibits the recovery of stranded generation costs in transmission rates. There is nothing on the face of the statute or in its legislative history to support this position. In fact, section 212(a) permits recovery of "legitimate, verifiable and economic costs" of providing transmission service. Stranded costs clearly are an economic cost of providing transmission when the stranding results from the ordered transmission service. By definition, the costs for which this Rule provides an opportunity for recovery would not have been stranded but for Commission-mandated transmission access. Stranded costs under this Rule are the costs that a utility incurred to provide service to a customer based on a reasonable expectation that the utility would continue to serve the customer beyond the term of their contract, and that become stranded when the customer uses Commission-mandated ***12398** transmission access to reach a new generation supplier. In this respect, stranded costs, like opportunity costs,[FN638] are not costs associated with the actual facilities used to provide transmission service. Rather, they are an "economic cost" of providing the transmission service at issue.

4. Recovery of Stranded Costs Associated With New Wholesale Requirements Contracts

In Order No. 888, we concluded that future wholesale requirements contracts should explicitly address the mutual obligations of the seller and buyer, including the seller's obligation to continue to serve the buyer, if any, and the buyer's obligation, if any, if it changes suppliers. This means that utilities must address potential stranded cost issues when negotiating new contracts or be held strictly accountable for the failure to do so.

We stated that we will allow recovery of wholesale stranded costs associated with any new requirements contract (executed after July 11, 1994, or extended or renegotiated to be effective after July 11, 1994) only if explicit stranded cost provisions are contained in the contract. We defined "explicit stranded cost provision" (for contracts executed after July 11, 1994) as a provision that identifies the specific amount of stranded cost liability of the customer(s) and a specific method for calculating the stranded cost charge or rate. However, for purposes of requirements contracts executed after July 11, 1994 but before May 10, 1996 (the date on which Order No. 888 was published in the Federal Register), we clarified that a provision that specifically reserved the right to seek stranded cost recovery consistent with what the Commission permits in the Final Rule (without identifying the specific amount of stranded cost liability of the customer(s) and calculation method) nevertheless will be deemed an "explicit stranded cost provision." On the other hand, a provision in a requirements contract executed after July 11, 1994 but before May 10, 1996 that merely postpones the issue of stranded cost recovery without specifically providing for such recovery will not be considered an "explicit stranded cost provision." We said that, after May 10, 1996, a provision must identify the specific amount of stranded cost liability of the customer(s) and a specific method for calculating the stranded cost charge or rate in order to constitute an "explicit stranded cost provision." [FN639]

We also concluded that a requirements contract that is extended or renegotiated for an effective date after July 11, 1994 becomes a "new" requirements contract for which stranded cost recovery will be allowed only if explicitly provided for in the contract.

We decided not to impose a regulatory obligation on wholesale requirements suppliers to continue to serve the power needs of their existing requirements customers beyond the end of the contract term. The only exception to this would be if the customer decides to remain a requirements customer for the period for which the Commission finds that the supplying utility reasonably expected to continue serving the customer. In such a case, the supplying utility will be obligated to offer continuing service to the requirements customer for the period the utility reasonably expected to continue serving the customer.

We also decided to no longer require prior notice of termination under section 35.15 for any power sales contract executed on or after July 9, 1996 (the effective date of the Final Rule pro forma tariff) that is to terminate by its own terms (such as on the contract's expiration date), but to require written notification of the termination of such contract within 30 days after termination takes place. We said that we will continue to require prior notice of the proposed termination of any power sales contract executed before July 9, 1996 (even if the contract is to terminate by its own terms) as well as any unexecuted power sales contract that was filed before that date.

Further, we decided to retain the section 35.15 filing requirement for all transmission contracts because the Commission must be assured that transmission owners are not exerting market power in negotiating or terminating transmission contracts. This filing requirement will provide the customer an opportunity to notify the Commission if the termination terms are disputed or if the customer was not given adequate opportunity to exercise its limited right of first refusal under the Final Rule (see Section IV.A.5).[FN640]

Requests for Rehearing

Utilities For Improved Transition asks the Commission either to clarify that it will enforce stranded cost provisions as agreed to by the parties and accepted for filing by the Commission (presumably even if they do not meet the definition of "explicit stranded cost provision" contained in the Preamble[FN641]), or to modify the definition contained in the Preamble (and add the term to the list of definitions in section 35.26(b)) to give contracting parties the option of specifying either a specific amount of stranded cost liability or a formula for calculating the stranded cost charge or rate. Utilities For Improved Transition contends that, particularly in the case of long-term contracts, the parties may not be able to quantify what the stranded cost liability will be at the time they enter into a contract.

Several entities assert that if the Commission is to permit recovery for stranded costs, it should include a symmetrical mechanism to permit customers with below-market rates or net undervalued assets a means to continue to receive power at below-market rates if the customer had a reasonable expectation of continued service.[FN642] OH Consumers' Counsel objects that the only exception in Order No. 888 to the Commission's decision not to impose a regulatory obligation on a utility to continue to serve existing requirements customers beyond the end of the contract "would be if the customer decides to remain a requirements customer for the period for which the Commission finds that the supplying utility reasonably expected to continue serving the customer."[FN643] According to OH Consumers' Counsel, this language nullifies the customer's reasonable expectation of continuation of service under its existing contractual arrangement.

TDU Systems similarly says that the Commission has not explained why the suppliers' expectations are to be honored, but the customers' expectations are not. TDU Systems objects that the Commission failed to explain why it rejected allowing requirements customers to demonstrate a reasonable expectation that they would continue to be able to obtain supplies of power at rates based on embedded cost after the expiration of ***12399** their supply contracts. TDU Systems submits that the case for providing extra-contractual relief to wholesale purchasers is more compelling than the case for providing extra-contractual relief to wholesale suppliers. It argues that it is likely that some cooperatives and municipal utilities would not survive the drastic impact to their businesses that the elimination of cost-based rates could bring.

OH Consumers' Counsel submits that the filing of a section 206 complaint by customers of utilities with rates below market does not provide adequate protection or symmetry for the customers. It contends that a section 206 case is an inadequate remedy because: (1) the utility holds all of the necessary information for analyzing such a case, but the procedure shifts the burden of proof from the utility to the customer; and (2) it provides only delayed relief for parties who could be irreparably harmed by the imposition of the market-based rates.

TDU Systems argues that eliminating the prior notice of termination requirement in section 35.15 for post-July 9, 1996 wholesale requirements contracts will result in discrimination and monopolization. It contends that the Commission closes its eyes to the fact that termination of a requirements contract can affect 100 percent of a customer's power supply, while it is likely to affect less than 10 percent of a large public utility's load. It submits that eliminating the prior notice of termination requirement is tantamount to finding that termination of all such contracts by their terms will be just and reasonable, but that no such finding can presently be supported. TDU Systems maintains that there remains significant market power in the markets in which transmission dependent utilities, especially small transmission dependent utilities, operate. It recommends that the Commission use section 35.15 to require that wholesale contracts not be terminated unless such termination is just and reasonable.

PA Munis objects that the Commission did not specifically address in Order No. 888 its proposal that contracts approved after July 11, 1994 (but executed before that date) be treated as new contracts. It submits that under the Commission's reasoning in setting the July 11, 1994 cut-off date, utilities that executed requirements contracts after that date had no reasonable expectation that they would be permitted to recover costs by seeking to amend the contract. It argues that the same reasoning applies where the contract was executed but not approved or accepted by the Commission by the July 11, 1994 notice date.

Commission Conclusion

We will clarify the definition of "explicit stranded cost provision" for requirements contracts executed after July 11, 1994. As long as the contracting parties are in agreement, a provision in a post-July 11, 1994 requirements contract will be considered an "explicit stranded cost provision" if it identifies either the specific amount of stranded cost liability of the customer or a specific method for calculating the stranded cost charge or rate.

We will reject the arguments of TDU Systems and OH Consumers' Counsel that "symmetry" requires that the Commission provide a generic mechanism in this Rule to allow existing requirements customers with below-market rates a means to continue to receive power beyond the contract term at the pre-existing contract rate if the customer had a reasonable expectation of continued service. Unlike the generic findings we have made with respect to extra-contractual recovery of stranded costs associated with requirements contracts executed on or before July 11, 1994, we do not have a sufficient basis on which to make generic findings that customers under such contracts may be entitled to extend a contract at the existing rate. Utilities' expectations may have resulted in millions of dollars of investments on behalf of certain customers and the possibility of shifting the costs of those investments to other customers that did not cause the costs to be incurred. In the case of customers' expectations, however, even if customers generally expected to stay on a supplier's system beyond the contract term, it is not likely that most customers could have expected to continue service at the existing rate unless specified in the contract. Moreover, the consequences of customers' expectations as a general matter would not have the potential to shift significant costs to other customers.

Nevertheless, our conclusion that we cannot make generic findings or provide a generic formula for addressing this issue does not mean that a customer under a contract may not exercise its procedural rights under section 206 to show that the contract should be extended at the existing contract rate,[FN644] or to make such a showing in the context of a utility's proposed termination of a contract pursuant to the section 35.15 notice of termination (approval) requirement, which we have retained for power supply contracts executed prior to July 9, 1996 (the effective date of the Rule).

We believe that while the relationship between utilities and their wholesale requirements customers may have given rise to an inference or expectation on the part of the wholesale requirements customer that the contract would continue beyond the stated term, it is not clear to what extent a customer could demonstrate a reasonable expectation that such continued service would be at the existing contract rate (which may be below the market price). This is particularly the case for contracts in which the utility has not waived its unilateral right to make section 205 filings to change the rates. Even in contracts where rates were fixed for the contract term, however, if the utility were to agree to extend such a contract for a new term, the rates under that contract would not necessarily have remained the same. On this basis, a customer may be able to demonstrate that it had a reasonable expectation of continued service beyond the contract term, but not necessarily at the same rate level. It is for this reason that we believe this issue must be addressed on a case-by-case basis and that this Rule is not the proper mechanism for granting the relief sought by TDU Systems and OH Consumers Counsel.

Nevertheless, we do not intend to prejudge whether a requirements customer could ever make a showing that it reasonably expected service beyond the contract term at the existing contract price. Nor do we intend to preclude a customer from attempting to make such a showing in appropriate circumstances.

We also believe that we adequately addressed in Order No. 888 TDU Systems' argument that elimination of the prior notice of termination requirement in section 35.15 for post-July 9, 1996, wholesale requirements contracts will result in discrimination and monopolization. As we stated in Order No. 888, we believe that the concerns of TDU Systems can be fully addressed without retaining the section ***12400** 35.15 prior notice of termination requirement for post-July 9, 1996 contracts. While we have agreed to provide for extra-contractual stranded cost recovery as a transition matter, it is our objective that, prospectively, parties should address their mutual expectations clearly through contract terms that explicitly address the mutual obligations of the seller and buyer at contract expiration. This would include the seller's obligation to continue to serve the buyer after contract expiration, if any. If the customer believes that termination of its contract at the end of the term would not be just and reasonable (or, in the case of a Mobile-Sierra contract, would not be in the public interest), it can file a complaint with the Commission under section 206 of the FPA.

We will reject PA Munis' request that contracts approved after July 11, 1994 (but executed before that date) be treated as "new" contracts for purposes of stranded cost recovery because modifying the notice date at this point in the proceeding would work an inequitable result. Beginning with the initial stranded cost NOPR, the Commission put entities on notice that contracts "executed" on or before July 11, 1994 would constitute "existing" contracts. Although a utility arguably could have amended such an existing contract to include an explicit stranded cost provision prior to its (post-July 11, 1994) approval by the Commission, the NOPR did not require the utility to do so. As a result, it would be unfair for the Commission to change the cut-off terms now.

5. Recovery of Stranded Costs Associated With Existing Wholesale Requirements Contracts

In Order No. 888,[FN645] the Commission concluded that it would permit utilities the opportunity to seek recovery of legitimate, prudent and verifiable stranded costs for "existing" wholesale requirements contracts (executed on or before July 11, 1994) that do not already contain exit fees or other explicit stranded cost provisions.[FN646] We explained why we believe that July 11, 1994—the date on which the initial Stranded Cost NOPR was published and, thus, on which the industry was put on notice of the proposal to disallow prospectively extra-contractual recovery of stranded costs—is the appropriate date for distinguishing "existing" requirements contracts from "new" requirements contracts.

We noted our desire that utilities attempt to renegotiate with their customers existing requirements contracts that do not contain exit fees or other explicit stranded cost provisions. If a contract is not renegotiated to add such a provision, we explained that, before the expiration of the contract: (1) A public utility or its customer may file a proposed stranded cost amendment to the contract under sections 205 or 206; or (2) a public utility in a section 205 proceeding, or a transmitting utility in a section 211 proceeding, may file a proposal to recover stranded costs associated with any such existing contract through its transmission rates for a customer that uses the utility's transmission system to reach another generation supplier.

We also concluded that, even if an existing requirements contract contains an explicit Mobile-Sierra[FN647] provision, it is in the public interest to permit the public utility to seek a unilateral amendment to add stranded cost provisions if the contract does not already contain exit fees or other explicit stranded cost provisions.[FN648] We explained why our determination that it is in the public interest to give public utilities a limited opportunity to propose contract changes unilaterally to address stranded costs if their contracts do not already explicitly do so satisfies the public interest standard of the Mobile-Sierra doctrine. We also indicated that customers with Mobile-Sierra contracts that do not explicitly address stranded costs may file complaints under section 206 of the FPA to propose to address stranded costs in existing requirements contracts.

We concluded that a public utility or its customer should be allowed to file a proposed stranded cost amendment, or a public utility or transmitting utility should be allowed to file a proposal to recover stranded costs through a departing generation customer's transmission rates, at any time prior to the expiration of the contract.

Rehearing Requests—July 11, 1994 Cut-Off Date

Utilities For Improved Transition, repeating an argument raised in previous comments in this proceeding, objects to the Commission's July 11, 1994 cut-off date for distinguishing between "existing" and "new" requirements contracts. It argues that stranded cost recovery should be assured for all contracts executed before the effective date of the Rule (i.e., July 9, 1996), not just those executed before July 11, 1994. It asserts that parties to contracts executed after July 11, 1994 but before July 9, 1996 should have the same opportunity as parties to pre-July 11, 1994 contracts to offer evidence as to their reasonable expectations. Utilities For Improved Transition asserts that agencies may not promulgate retroactive rules without express statutory authority, [FN649] and that the FPA does not give the Commission such statutory authority.

Puget raises a somewhat different point. It notes that the definition of a "new" requirements contract as "any wholesale requirements contract * * * extended or renegotiated to be effective after July 11, 1994" (emphasis added) was not proposed until March 29, 1995 (in the supplemental stranded cost NOPR). Puget states that the initial stranded cost NOPR proposed to give a utility three years from the date of Federal Register publication of the final stranded cost rule to negotiate or to file for stranded cost recovery. According to Puget, the March 1995 supplemental stranded cost NOPR proposed a retroactive change by defining a contract executed prior to July 11, 1994 but extended or renegotiated to be effective after that date as a "new" contract and by removing the three-year window for negotiating stranded cost recovery. By this change, Puget argues that the extension of a contract between the date of Federal Register publication of the initial NOPR (July 11, 1994) and the issuance of the supplemental NOPR (March 29, 1995) may have converted it into a "new" rather than an "existing" ***12401** contract for stranded cost recovery purposes. Puget asks the Commission to revise the definition of "existing wholesale requirements contract" in Order No. 888 and 18 CFR 35.26 to include contracts executed on or before July 11, 1994 that were extended prior to the issuance of the supplemental stranded cost NOPR (March 29, 1995) and for which stranded cost provisions were filed with the Commission prior to issuance of Order No. 888. Puget submits that failure to do so would be arbitrary and capricious and would deprive utilities with such contracts of adequate notice of a proposed rule.[FN650]

Commission Conclusion

We will reject Utilities For Improved Transition's rehearing request because we believe that we adequately explained in Order No. 888 why adoption of the July 11, 1994 cut-off date is appropriate and does not constitute retroactive rulemaking. We said in Order No. 888 that because all parties were put on notice in the initial stranded cost NOPR that July 11, 1994 would be the operable date for the "existing"/"new" contract distinction, utilities that executed requirements contracts after that date could have had no reasonable expectation that they would be permitted to recover any costs extra-contractually. Moreover, we explained that because the costs at issue are extra-contractual costs, the Commission's notice to all parties that contracts executed after July 11, 1994 (the date that the initial NOPR was published in the Federal Register) will be enforced by their terms as far as stranded cost recovery is concerned does not constitute "retroactive rulemaking." The Commission has merely put all parties on notice that the opportunity for extra-contractual stranded cost recovery would not be available for any requirements contracts executed after July 11, 1994.

The July 11, 1994 date is appropriate because it is the date on which all interested parties were given notice in the Federal Register that the recoverability of stranded costs for contracts executed on or before that date that did not provide for such recovery was at issue. The parties to requirements contracts executed after July 11, 1994 have been free to provide for stranded cost recovery in the contract, or not. The point is that, for requirements contracts executed after the cut-off date, stranded cost recovery will be governed solely by the terms of the contract.

We believe that Puget has raised a valid point concerning the potential impact of the Commission's decision in the March 29, 1995 supplemental stranded cost NOPR to treat extensions or renegotiations of existing contracts as "new" contracts for stranded cost purposes on parties that extended or renegotiated an existing contract prior to March 29, 1995. However, we expect that the situation described by Puget may be an isolated instance. On this basis, we do not believe it necessary to modify the definition of "existing wholesale requirements contracts" in Order No. 888 and 18 CFR 35.26 as requested by Puget. Nevertheless, we clarify that we will consider on a case-by-case basis whether to waive the provisions of 18 CFR 35.26 and to treat a contract extended or renegotiated (without adding a stranded cost provision) to be effective after July 11, 1994 but before March 29, 1995 as an existing contract for stranded cost purposes.[FN651]

Rehearing Requests—Mobile-Sierra

Several entities challenge the Commission's generic Mobile-Sierra public interest finding. According to APPA, the Commission cannot make the public interest determination in a generic rulemaking, whether for stranded cost or non-stranded cost modifications.

A number of entities object that the Commission does not identify any utilities whose existence is jeopardized without full wholesale stranded cost recovery.[FN652] PA Munis and APPA assert that vague allegations of harm if utilities do not recover stranded costs do not satisfy the public interest standard which they view to be "practically insurmountable."[FN653] American Forest & Paper contends that there is not one fact to support the Commission's assumption about threats to the financial stability of the electric utility industry. ELCON submits that significant retail stranded cost exposure does not justify the rule on wholesale stranded cost recovery.

VT DPS and Valero submit that the Commission has not explained how allowing utilities to abrogate their contracts to extract exit fees from former customers vindicates any public interest. They argue that even assuming that wholesale customers depart en mass, the customers can only do so as their contracts expire; thus, the exodus, if it occurs, will be a trickle, not a flood. VT DPS and Valero maintain that even if some utilities were put at risk, it would not justify a generic rule. They contend that based on AGD v. FERC,[FN654] a generic solution is not proper for a problem existing only in "isolated pockets."

PA Munis submits that, even assuming that the financial integrity of some utilities may be threatened, the missing link in the Commission's logic for a generic rule is that there is no protection for customers having Mobile-Sierra contracts with public utilities that are not faced with financial problems or cost shifting to third parties as a result of the open access requirements. PA Munis asserts that, at a minimum, each utility having Mobile-Sierra contracts should be required to show on an individual basis that the public interest standard has been satisfied.

American Forest & Paper argues that Order No. 888 is not made even-handed by allowing requirements customers to also challenge fixed-rate, fixed-term contracts. It submits that letting a customer file to amend a contract only as long as that amendment also addresses stranded costs is a "heads you win, tails I lose" proposition for the customer.

APPA and TDU Systems request clarification of the scope of the Commission's decision to allow a utility "to seek modification of contracts that may be beneficial to the customer" if the customer is permitted to argue for modification of existing contracts that are less-favorable to it than other generation alternatives. APPA expresses concern that this language could be interpreted to mean that once a ***12402** customer seeks modification of stranded cost provisions in an existing contract, the utility may be able to challenge its entire contract with the customer. If this means the utility can modify contract provisions unrelated to stranded costs, APPA submits that the Commission has failed to address the Mobile-Sierra public interest issues associated with modifying non-stranded cost provisions in an existing contract. If not, APPA contends that the Commission should clarify the language. APPA objects that the Commission has not placed any limits on the types of modifications that a selling utility can make, nor specified the types of changes that it thinks a utility will likely make. It states that the Commission needs to explain why joint modification by both the seller and the purchaser can meet the public interest standard. According to APPA, the Commission has not explained the need for symmetrical treatment of contracts negotiated at a time when the Commission has found that the supplying public utilities were exercising their monopoly over transmission facilities in an unduly discriminatory manner.

APPA also contends that the Commission's reliance on Northeast Utilities[FN655] is misplaced because that case involved the Commission's review of a newly-filed contract, as opposed to subsequent review of a contract previously accepted and approved by the Commission. APPA further asserts that Northeast Utilities involved an affiliate transaction, whereas this rulemaking is targeted at arm's-length agreements between unrelated selling and purchasing utilities. According to APPA, this rulemaking does not present any of the concerns at issue in an affiliate transaction, and the Commission should have applied the "practically insurmountable" public interest standard doctrine from Papago, the classic "low-rate" case.

Commission Conclusion

We disagree with those entities that argue that the Commission cannot make the public interest determination in a generic rulemaking. It is well established that it is within the Commission's discretion to decide whether we act through rule or through case-by-case adjudications.[FN656] As we explained in Order No. 888, we believe it is appropriate that our public interest finding be made on a generic basis given the fact that, by this Rule, we are requiring full open access that could significantly affect historical relationships among traditional utilities and their customers and the ability of utilities to recover prudently incurred costs.

At the same time, however, we are not eliminating the need for case-by-case demonstrations that stranded cost recovery should be allowed. Our public interest finding is that utilities be permitted to seek extra-contractual recovery of stranded costs in certain defined circumstances and that they be allowed to recover stranded costs only if they make a case-specific demonstration.

Our holding applies only to wholesale requirements contracts (with Mobile-Sierra clauses) executed on or before July 11, 1994 that do not contain an exit fee or other explicit stranded cost provision. We will not permit modification of any contract that addresses the stranded cost issue explicitly, unless the contract specifically permits such modifications. Instead, we are examining requirements contracts that do not clearly address the issue in the context of the traditional regulatory regime under which they were signed—a regulatory environment in which it was assumed as a matter of course that the great majority of requirements customers would stay with their original suppliers and that these suppliers had a concomitant obligation to plan to supply these customers' continuing needs.

Further, utilities with Mobile-Sierra contracts that seek recovery of stranded costs will have the burden, on a case-by-case basis, of showing they had a reasonable expectation of continuing to serve the departing generation customer. Although we have decided on a generic basis that it is in the public interest to permit public utilities with Mobile-Sierra contracts to make unilateral filings, we are not automatically approving any amendment that a particular utility might file. If a public utility unilaterally files a proposed stranded cost amendment under either section 205 or 206 of the FPA, this does not necessarily mean that the Commission will find it appropriate to allow such amendment. In addition, customers with Mobile-Sierra contracts that do not explicitly address stranded costs may also file complaints under section 206 of the FPA to propose to address stranded costs in existing requirements contracts. The Commission will analyze any proposed stranded cost amendment to a Mobile-Sierra contract, whether proposed by the utility or by its customer, based on the particular circumstances surrounding that contract. Thus, the case-by-case findings that some commenters seek will, in effect, be made when the Commission determines whether to approve a proposed stranded cost amendment to a particular contract.[FN657]

Although several entities have raised various challenges to the sufficiency of the Commission's public interest finding, we believe that we have satisfied the public interest standard by showing how third parties may ultimately bear the burden if public utilities with Mobile-Sierra contracts are not given any opportunity to propose contract changes to address stranded costs.[FN658] As we explained in Order No. 888, if the Commission fails to give a public utility this opportunity, and the utility's financial ability to continue the provision of safe and reliable service is impaired, third parties (customers relying on the public utility for their electric service) will be placed at risk. Similarly, if the Commission fails to give a public utility the opportunity to directly assign costs to the customers on whose behalf they were incurred, and some of the utility's customers leave the utility's generation system for that of another supplier without paying such costs, third parties (the utility's remaining customers) may be harmed by having to bear costs that were not incurred to serve them and that are stranded by the other customers' departures via open access transmission. We believe that protective action in the public interest is particularly necessary where, as here, a utility's rates could become insufficient because of fundamental changes in the industry that largely result from legislative or regulatory changes that could not be anticipated.

In response to those entities that contend that speculation of financial jeopardy or generalized statements of what may occur without reference to particular public utilities is not sufficient to satisfy the public interest standard, we disagree. The Commission need not make findings about particular utilities because the Rule does not ***12403** award stranded costs—it simply sets out generic criteria for determining recovery in a particular case. If a utility does not meet the criteria, there will be no stranded cost recovery. The public interest determination rests on the obvious conclusion that the failure of a utility to recover costs prudently incurred and financed based on investor expectation of traditional cost recovery clearly adds regulatory risk that investors reasonably did not expect.

VT DPS's and Valero's reliance on AGD as support for the proposition that, even if some utilities were put at risk, a generic solution is not proper for a problem existing only in "isolated pockets" is misplaced. The AGD court found that the Commission had not adequately justified its decision to give all bundled firm sales customers of a pipeline that decided to offer service under Order No. 436 the option to reduce their contract demand by 100 percent. In noting the lack of support for "an industry-wide solution for a problem that exists only in isolated pockets," the court expressed concern that the remedy adopted by the Commission ("such drastic action as 100% CD reduction"[FN659]) was too broad.

In Order No. 888, in contrast, the Commission has determined that it is in the public interest to give a limited class of utilities —those that are parties to wholesale requirements contracts that were executed on or before July 11, 1994 that do not contain an exit fee or other explicit stranded cost provision and that contain Mobile-Sierra clauses—an opportunity to seek to add a stranded cost provision to the contract. Thus, the narrow scope of the Commission's Mobile-Sierra public interest finding is a far cry from the broad remedy (100 percent CD reduction) that the court remanded in AGD. Indeed, it more closely resembles the type of limited generic action that the AGD court suggested would be proper when it stated: "This is not to say, of course, that the Commission could not use generic rules to identify a limited class of LDCs to be entitled to reduce CD when special conditions are present."[FN660]

We explained in Order No. 888 that we were making two complementary public interest findings. First, as described above, is our decision that it is in the public interest to permit public utilities to seek stranded cost amendments to existing requirements contracts with Mobile-Sierra clauses. Second, we found that a "party" to a requirements contract containing a Mobile-Sierra clause no longer will have the burden of establishing independently that it is in the public interest to permit the modification of such contract, but still will have the burden of establishing that such contract no longer is just and reasonable and therefore ought to be modified. We clarify that, in making this second finding, our reference to a "party" to a requirements contract containing a Mobile-Sierra clause was directed at modification of contract provisions by customers.[FN661] Additionally, this second finding applies to any contract revisions sought, whether or not they relate to stranded costs.[FN662]

We also concluded that "if a customer is permitted to argue for modification of existing contracts that are less favorable to it than other generation alternatives, then the utility should be able to seek modification of contracts that may be beneficial to the customer."[FN663] We clarify in response to APPA and TDU Systems that this statement was not intended to imply that the Commission had made Mobile-Sierra findings that would permit utilities with Mobile-Sierra contracts to seek non-stranded cost amendments to contracts that may be favorable to a customer, based on a showing that the contracts are no longer just and reasonable. Our Mobile-Sierra findings as to public utility sellers apply only when utilities seek to add stranded cost provisions or make other modifications related to stranded costs. Thus, if a utility with a Mobile-Sierra contract initiates a section 206 proceeding in which it seeks to modify contract provisions that do not relate to stranded costs, it will have to show that it is contrary to the public interest not to modify the contract.

As we stated in Order No. 888, the most productive way to analyze contract modification issues is to consider simultaneously both the selling public utility's claims, if any, that it had a reasonable expectation of continuing to serve the customer beyond the term of the contract and the customer's claim, if any, that the contract no longer is just and reasonable and therefore ought to be modified. We said that if a customer brings a claim in a section 206 proceeding to shorten or terminate a contract, the selling public utility must bring any stranded cost claim with respect to that customer in that section 206 proceeding. Our goal is to ensure that all of the issues expected to be raised by the parties when a customer departs a utility's generation system can be efficiently litigated in one proceeding. Therefore, we have similarly required that if the customer intends to claim that the notice or termination provision of its existing requirements contract is unjust and unreasonable, it must present that claim in any proceeding brought by the selling public utility to seek recovery of stranded costs. We disagree with American Forest & Paper's argument that it is a "no-win" situation if a customer seeking to modify a contract must present that claim in any stranded cost proceeding brought by the selling public utility. To the contrary, providing the customer to a Mobile-Sierra contract with the opportunity to demonstrate that its contract is no longer just and reasonable and that its term should be shortened or eliminated could be beneficial to the customer, notwithstanding the customer's potential stranded cost obligation. As we explained in the Rule:

[G]iven the industry circumstances now facing us, both selling utilities and their customers ought to have an opportunity to make the case that their existing requirements contracts ought to be modified. By providing both buyers and sellers this opportunity, the Commission attempts to strike a reasonable balance of the interests of all market participants.[FN[664]]]

In response to APPA's analysis of Northeast Utilities, it is true, as APPA asserts, that Northeast Utilities involved the Commission's initial review of a contract, not modification of a previously accepted and approved contract, and that the contract involved an affiliate transaction, while this rulemaking is targeted at arm's-length agreements. However, we do not believe that these differences bear on the precedential value of this case to the circumstances presented in the Rule. To the contrary, we believe that Northeast Utilities provides valuable guidance concerning application of the public interest standard where, as here, a failure to allow limited contract modification may harm the public interest by harming third parties.

We disagree with APPA's contention that the Commission should have applied the "practically ***12404** insurmountable" standard from "the classic 'low-rate' case, namely, Papago."[FN665] As we have stated on several occasions, "we do not interpret the public interest standard of review * * * as imposing on us a practically insurmountable burden in situations in which we are protecting non-parties to a contract."[FN666] Additionally, we do not interpret the public interest standard as practically insurmountable in extraordinary situations such as this one where historic statutory and regulatory changes have converged to fundamentally change the obligations of utilities and the markets in which they and their customers will operate. In this circumstance, we believe the public interest test is met where the Commission determines that it is necessary to allow parties to seek contract amendments in order to protect the stability and financial integrity of the electric industry in general during the transition to competition as well as the interest of third parties affected by the transition. This type of situation simply was not addressed in Papago.

Congress has entrusted the Commission with the statutory responsibility to protect the public interest. As we explained in Northeast Utilities Service Company:[FN667]

Protection of the 'public interest' provides the justification for the Commission's power to regulate public utilities under Part II [of the FPA]. Specifically, section 201(a) of the FPA declares 'that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest' and that federal regulation of matters related to generation (to the extent provided in Parts II and III of the FPA) and of the transmission and sale at wholesale of electric energy in interstate commerce 'is necessary in the public interest.'

Consistent with our statutory obligations under the FPA, the Commission has an overriding responsibility to protect non-parties affected by Mobile-Sierra contracts, including consumers, to ensure that matters entrusted to our jurisdiction function smoothly during the restructuring transition, and to fairly balance the interests of utilities and customers during the transition. [FN668] The ability to meet our overarching public interest responsibilities would be virtually precluded if we must apply a practically insurmountable standard of review before we can take action to address industry-wide transition issues.

Rehearing Requests Supporting Limited Transition Period

Several entities request rehearing of the Commission's decision not to establish a three-to five-year period within which stranded cost recovery could be raised. They assert that if the Commission truly views stranded investment as a transition process, the transition should not be an extended one.[FN669]

Commission Conclusion

The Commission will deny the requests for rehearing on this point. As we explained in Order No. 888, although we considered limiting the period within which stranded cost recovery could be raised, there is no uniform time remaining on requirements contracts executed on or before July 11, 1994. [FN670] As a result, any limitation on the period in which parties could propose amendments covering stranded costs, such as three years, would affect market participants unequally. Those with long terms remaining on their contracts could object that immediately addressing the issue would not be cost effective. A utility with a long remaining term might not even seek stranded cost recovery depending on the competitive value of its assets near the end of the contract term.[FN671] However, such a utility would invariably seek to preserve its option to seek stranded cost recovery if its failure to do so within a short period resulted in a waiver of its right to do so. Having determined that it is generally appropriate to leave in place existing requirements contracts, it is not then reasonable to create a time limitation on stranded cost recovery that would encourage a supplier to seek early termination in order to preserve its stranded cost recovery rights.

On this basis, we believe that we have adequately explained the rationale for our decision to allow stranded cost claims to be raised at any time prior to the termination of the contract, instead of within three to five years of the effective date of the Rule.

6. Recovery of Stranded Costs Caused by Retail-Turned-Wholesale Customers

In Order No. 888, we concluded that this Commission should be the primary forum for addressing the recovery of stranded costs caused by a retail-turned-wholesale customer.[FN672] We stated that if such a customer is able to reach a new generation supplier because of the new open access (through the use of a FERC-filed open access transmission tariff or through transmission services ordered pursuant to section 211 of the FPA), any costs stranded as a result of this wholesale transmission access should be viewed as "wholesale stranded costs." We explained that there is a clear nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs and that, in these circumstances, this Commission should be the primary forum for addressing recovery of such costs. [FN673]

We said we will not be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory. We indicated that in these situations there is no direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs. The risk of an existing municipal utility expanding its territory was a risk prior ***12405** to the Energy Policy Act and prior to any open access requirement.

Nevertheless, we did express concern that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission—either this Commission or state commissions—to address recovery of stranded costs. We reserved the right to address such situations on a case-by-case basis.

Rehearing Requests Opposing Retail-Turned-Wholesale Jurisdiction

A number of entities challenge the Commission's assertion that costs associated with retail-turned-wholesale customers would not be stranded but for the FERC-jurisdictional transmission access requirement. They assert that the condition precedent to municipalization is the operation of a state process, and thus that it cannot be the case that the recovery of costs caused by a retail-turned-wholesale customer is "not subject to regulation by the States." They submit that such costs would not be stranded but for the action of state legislators or state regulators in granting authority for the customer's status change. They argue that any nexus that the Commission's authority under the FPA has to wholesale transmission services subsequently provided to the new wholesale customer is entirely derivative of the state's action.[FN674]

A number of entities argue that jurisdiction over costs that are stranded when a retail customer becomes a wholesale customer should be left to the states because the facilities used to provide retail service to these retail customers were subject to state jurisdiction and were included in retail rate base when the service was rendered.[FN675] They argue that because the Commission had no jurisdiction over the public utility facilities and costs incurred to serve retail-turned-wholesale customers, it has no jurisdiction to address those public utility costs if they become stranded. Thus, according to these entities, the conversion of the customer from retail to wholesale does not simultaneously effectuate a conversion of the costs from retail to wholesale.

AR Com and MO/KS Coms submit that jurisdiction over the costs incurred for historical retail customers does not shift unless the parties themselves make those costs a part of their new wholesale contract. NY Com submits that the Commission should recognize the states' jurisdiction to set the level of stranded costs associated with retail-turned-wholesale customers to be recovered in wholesale transmission rates set by FERC. FL Com asserts that state authorities are in a better position to assess the extent of stranded facilities and their costs, and that the Commission's involvement should be limited to that requested by a state by petition.

OH Com states that the Commission's position on stranded costs associated with retail-turned-wholesale customers invites second-guessing of state commission determinations and encourages forum shopping by introducing more than one stranded cost treatment within a single state jurisdiction. It expresses concern that utilities may seek to creatively disaggregate into generation, transmission, and distribution companies in ways to deliberately recast traditional retail relationships as wholesale in an effort to obtain favorable regulatory treatment of stranded costs.

IN Com submits that Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers will discourage state legislatures from making municipalization more available. VT DPS and Valero argue that the threat of a stranded cost surcharge will erect a new barrier to the formation of municipal utilities. They note that the Rule refers to one commenter's observation that, if Otter Tail could have made a stranded cost claim against the municipal utility that Elbow Lake planned to create, Otter Tail would not have needed to refuse to wheel and there would never have been an Otter Tail case. They submit that the Commission never addressed whether, or why, it believed the point to be wrong.

VT DPS and Valero also assert that the Rule represents a major inconsistency with prior Commission treatment of municipalization. They submit that the Commission historically promoted franchise competition between municipalities and utilities by holding tariff provisions that restrict such competition to be anticompetitive and unreasonable.[FN676]

American Forest & Paper submits that recovery of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's actions in the natural gas industry, where the Commission has encouraged competition at the retail level through competitive bypass and has not created barriers to competitive entry by imposing transition charges or exit fees on converting customers.[FN677]

Nucor objects that the Rule does not address the substantive findings, the common sense rationale, or the jurisdictional distinction drawn in United Illuminating.[FN678] It contends that the Commission's observation in Order No. 888 that there may not be a state regulatory forum for the recovery of stranded costs associated with retail-turned-wholesale customers and hence that the Commission should be the primary forum for addressing such stranded costs is flawed because there always is a state forum to address such cost recovery (the adequacy of the relief provided is a very distinct issue) and open access transmission does not and cannot cause retail competition to occur.[FN679]

Commission Conclusion

We will reject the requests for rehearing of our decision to be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers. We find the requests for rehearing on this issue unpersuasive. While it may be the case, as some entities suggest, that state action is a condition precedent to municipalization, the rehearing petitions ignore the fact that the Rule covers situations in which open access is also a condition precedent to the municipalized customers leaving their existing supplier's system. Order No. 888 does not propose that the Commission be the primary forum for stranded cost recovery for all cases of municipalization. Instead, our holding is limited to those cases in which the new wholesale entity uses Commission-mandated transmission access to obtain new power supply on behalf of retail customers that were formerly supplied ***12406** power by the utility providing the transmission service.[FN680]

As we explained in Order No. 888, in such cases there is a direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of costs stranded as a result of this wholesale transmission access. Thus, the stranded costs associated with retail-turned-wholesale customers for which Order No. 888 provides an opportunity for recovery would not have been incurred but for the action of this Commission in requiring a utility to make unbundled transmission services available. In these cases, the former bundled retail customers of the historical supplying utility (now the bundled retail customers of the new municipal system) would not have obtained access to new power supply but for the Commission's order mandating transmission. Without the regulatory mandate to provide access, the utility would have indirectly continued sales to the same retail customers because the new municipal utility purchasing power on the retail customers' behalf would have had no way to reach other power suppliers. In this situation, there would be no stranded generation costs. In other words, the creation of a municipal utility intermediary to purchase power at wholesale would not, by itself, trigger stranded costs. Rather, it is the access from the historical supplier of the bundled retail customers that is the condition precedent to reaching other power suppliers and thereby triggering stranded costs. Therefore, there is a clear causal nexus between the stranded costs and the availability and use of the tariff required by the Commission.

Costs that are exposed to nonrecovery when a retail customer or a newly-created wholesale power sales customer ceases to purchase power from the utility and does not use the utility's transmission system to reach a new generation supplier (e.g., through self-generation or use of another utility's transmission system) do not meet the definition of "wholesale stranded costs" for which the Rule provides an opportunity for recovery. Such costs are outside the scope of the Rule because such costs would not be stranded as a direct result of the new open access.

In response to the argument that conversion of a customer from retail to wholesale would not simultaneously effectuate a conversion of the costs from retail to wholesale, we believe this argument confuses the issue. We note that we have defined stranded costs as wholesale or retail on the basis of whether wholesale or retail open access is the cause of the costs being stranded, not on the basis of the original retail or wholesale characteristic of the costs. Thus, even though costs may have been originally incurred as retail-related costs, the precipitating event that results in such costs being stranded in the retail-turned-wholesale customer scenario is the use by the new wholesale customer of the Commission-mandated tariff. When a customer is able to use the Commission-required tariff to reach another generation supplier, it causes the utility to incur an economic cost in providing transmission service that is equal to the foregone revenues that the utility reasonably expected to receive under a state regulatory regime. Thus, because of the causal nexus between the use of a former supplying utility's Commission-mandated transmission tariff and the potential for foregone revenues by that utility as a result of the Commission-required access, the costs stranded by a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In response to those entities that express concern that the Commission's position on stranded costs associated with retail-turned-wholesale customers invites second-guessing of state commission determinations, we emphasize that we have assumed primary authority to address such costs only in a limited category of cases where there is a direct nexus between the availability of Commission-required open access and the stranding of costs when the former customer uses the former supplying utility's transmission system (through its open access tariff or a section 211 order) to reach a new supplier. We indicated in Order No. 888 that if the state has permitted any recovery from departing retail-turned-wholesale customers, such amount will not be stranded for purposes of this Rule. We will deduct that amount from the costs for which the utility will be allowed to seek recovery under this Rule from the Commission. In so doing, however, we are not second-guessing the states as to what a utility may recover under state law. Additionally, we will give great weight in our proceedings to a state's view of what might be recoverable.

We also reject the argument that the Commission's position on stranded costs associated with retail-turned-wholesale customers encourages forum shopping. To the contrary, as we said in Order No. 888, to avoid forum shopping and duplicative litigation of the issue, we expect parties to raise claims before this Commission in the first instance. We believe that this Commission should be the primary forum because, without the open access provided by the Rule, the new municipal utility would not be able to reach a new supplier and, as a result, would not cause the utility to incur stranded costs (as defined in this Rule).

We reject as misplaced arguments that the Rule represents a major inconsistency with the Commission's historical promotion of franchise competition between municipalities and utilities and that it will discourage municipalization.[FN681] It continues to be the Commission's policy to encourage competition. Indeed, the goal of Order No. 888 is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers. However, the purpose of the stranded cost policy is neither to encourage nor to discourage municipalization, but rather to facilitate a fair transition to competition and to ensure stability in the industry during that transition. As we discuss elsewhere in this order, we believe that this Commission must address the recovery of the costs of moving from a monopoly-regulated regime to one in which all sellers can compete on a fair basis and in which electricity is more competitively priced. On this basis, we believe that if a new wholesale entity such as a municipal utility uses Commission-required open access to reach a new supplier on behalf of its retail customers (previously retail customers of the former supplier), the former supplying utility should be given an opportunity to recover legitimate, prudent and verifiable costs that it ***12407** incurred under the prior regulatory regime to serve that customer.

In response to American Forest & Paper's argument that recovery of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's policy in the natural gas industry of allowing competitive bypass without imposing transition charges or exit fees on converting customers, we note that industrial gas customers who bypass a local distribution company's (LDC) facilities do not escape transition costs quite so easily as suggested by American Forest & Paper. It is true that, when the end user bypasses the LDC to reach an interstate pipeline different from the pipeline serving the LDC, the Commission views the bypass as a risk of competition from which the LDC should not be shielded.[FN682] However, when the end user bypasses the LDC to reach the same interstate pipeline that serves the LDC, the Commission may take certain actions to minimize adverse effects on the LDC and its remaining customers.[FN683] Moreover, an end user that bypasses an LDC to reach the same pipeline that serves the LDC would, in any event, be allocated a share of the pipeline's gas supply realignment costs (if any), since those costs are allocated based on current contract demand (or usage).[FN684] Accordingly, we see no inconsistency between our bypass policy for the natural gas industry and Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers. Similar to our refusal to shield LDCs from the adverse effects of an end user's bypass to reach a different pipeline than serves the LDC, Order No. 888 does not provide an opportunity for stranded cost recovery where a retail-turned-wholesale customer uses another utility's transmission system to reach a new supplier. As we note above, the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers is limited to those cases in which the former retail customer obtains (either directly or through another wholesale transmission purchaser) unbundled transmission services from its former supplying utility. In the case of an end use customer bypassing the LDC to reach the same pipeline that serves the LDC, the end use customer would similarly be allocated a share of the pipeline's gas supply realignment costs. As a result, American Forest & Paper's attempt to rely on the Commission's gas bypass policy is misplaced.

We also disagree with those entities that argue that the Commission has failed to adequately distinguish Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers with the Commission's decision in United Illuminating. As we stated in Order No. 888, we recognize that we took a different approach to stranded cost recovery associated with retail-turned-wholesale customers in United Illuminating, where we suggested that state and local regulatory authorities or the courts should be able to provide an adequate forum to address retail franchise matters, including recovery of stranded costs caused by municipalization, but said we would consider revisiting the question if United Illuminating could demonstrate the lack of a forum.[FN685] However, we explained that since the issuance of that decision we have had an opportunity to re-analyze the nature of the stranded cost problem when a retail customer becomes a wholesale customer, including the potential that there might not be a state regulatory forum for recovery of such costs. In these circumstances, we have determined that where such costs are stranded as a direct result of Commission-mandated wholesale transmission access, these costs should be viewed as costs of the transition to competitive wholesale bulk power markets and this Commission should be the primary forum for addressing their recovery.

In response to Nucor's objection that there always is a state forum to address stranded cost recovery associated with retail-turned-wholesale customers, with the adequacy of the relief being a distinct issue, we clarify that our primary concern in retail-turned-wholesale situations is not whether there is an adequate state regulatory forum for the recovery of stranded costs associated with retail-turned-wholesale customers. Rather, our primary concern is that wholesale customers (whether or not formerly retail) should be responsible for the costs incurred to meet their power needs that are stranded when they use the wholesale transmission ordered by this Commission to reach new suppliers. Our decision to be the primary forum in the case of stranded costs associated with retail-turned-wholesale customers is based on the causal nexus between regulatory-mandated wholesale transmission access and the stranding of costs when a new municipal utility uses such access to obtain new power supply on behalf of retail customers previously served by the former supplying utility.

Rehearing Requests Seeking Expansion of Retail-Turned-Wholesale Jurisdiction

Other entities seek rehearing of the Commission's decision not to be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory.[FN686] A number of them argue that the loss of existing retail customers through municipal annexations or expansions is no different from the loss of retail customers through new municipalization because existing municipal systems are likely to use Commission-jurisdictional open access transmission to obtain resources to supply power to the annexed loads.[FN687] They submit that, just as with newly-municipalized customers, such costs would not be stranded but for the action of this Commission.

Some of these entities express concern that the Rule will encourage retail-turned-wholesale transactions to be undertaken as annexations rather than through the formation of new entities to avoid stranded costs. [FN688] Public Service Co of CO contends that Order No. 888, in conjunction with the Commission's section 211 order in American Municipal Power Ohio, Inc.,[FN689] may facilitate municipal annexations by enabling municipal systems to serve new territory through the establishment of second delivery points.

Coalition for Economic Competition and Puget also argue that the Commission must consider stranded *12408 costs that arise from municipal expansion in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. They contend that there is no justification for charging one rate to former retail customers taking transmission services through a new municipal utility and another rate to those taking service through municipal annexation or through use of another utility's transmission system.

PSE&G suggests that the distinction between new municipalization on the one hand and municipal annexation or expansion on the other hand may lead to unnecessary controversy and litigation as entities wrangle over whether a given expansion/annexation is really an expansion or a municipalization. It says that a situation could arise where a municipality serves one town in order to serve thousands of additional customers in a second town. According to PSE&G, it is not clear from the Rule whether the Commission would consider this an expansion of a municipality's service territory or a new municipalization.

Puget submits that the stranded cost recovery mechanism must not be subject to being frustrated by simple artifices such as having the new supplier (instead of the departing customer) request and contract for transmission service. SoCal Edison seeks clarification of the Commission's authority to mandate stranded cost recovery if a retail customer disconnects from a utility's system and accesses another generation supplier by interconnecting with a public power entity (who in turn would interconnect with a neighboring jurisdictional utility). It asks the Commission to clarify that such a transaction effectively constitutes a municipalization, not an expansion of a service territory, and that the Commission, under FPA section 211, can compel the recovery of stranded costs by having the "new" jurisdictional utility assess a stranded cost charge and pass the revenues on to the utility from whose system the customer departed.

SoCal Edison seeks several additional clarifications. It states that it understands that the Commission's primary forum status in no way prevents or interferes with a state's authority to order stranded cost recovery from departing retail customers. If this is not the case, SoCal Edison seeks rehearing on this issue. SoCal Edison also asks the Commission to clarify that the Commission retains the discretion to defer to a state stranded cost calculation methodology if appropriate to do so on the facts of a particular case.

Commission Conclusion

We have carefully reviewed the arguments made by petitioners seeking rehearing of our decision not to be the primary forum for stranded cost recovery in the case of municipal annexations. Based on that review we have decided to reconsider our decision. This conclusion is based in large part upon the very significant similarities between the creation of a new municipal utility system (also referred to as municipalization) and the expansion of an existing municipal utility system (e.g., through annexation of additional retail service territory). We recognize that the same nexus to Commission-required transmission access that forms the basis for our decision to allow a utility to seek stranded cost recovery in cases of new municipalization—use of the former supplying utility's transmission system—is likely to be present in some cases of municipal annexation. In the case of both new municipalizations and annexations, the bundled retail customers of a local utility become the bundled retail customers of a municipal utility (in one case a new municipal utility, in the other an existing municipal utility) that will use the transmission system of the retail customers' former supplier in order to access other suppliers.

As we explain above, in a "retail-turned-wholesale customer" situation, such as the creation of a municipal utility system, a newly-created entity becomes a wholesale power purchaser on behalf of the retail customers. It is the conduit by which retail customers, if they cannot obtain direct retail access, can reach power suppliers other than their historical local utility power supplier. Although the retail customers remain bundled retail customers, in that they become the bundled customers of the new entity, we call this a "retail-turned-wholesale customer" situation because the new entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply. The same analogy applies to newly-annexed customers; they become "new" wholesale customers in the sense that the wholesale entity obtains transmission and new power supply on their behalf.

Accordingly, we clarify that this Commission will be the primary forum for addressing the recovery of stranded costs if an existing municipal utility uses the transmission system of its annexed retail customers' former supplier to access new suppliers to serve the annexed load. As long as Commission-required transmission access (the former supplier's open access tariff or transmission services ordered under FPA section 211) is the vehicle that enables an existing municipal utility to obtain power supplies to serve annexed loads, we believe that any costs stranded as a result of this wholesale transmission access are properly viewed as economic costs that are jurisdictional to this Commission. In such a case, the bundled retail customers that are annexed by an existing municipal utility would, through the municipal utility, use the transmission system of their former supplier to obtain access to new supplies and thereby expose their former supplier to non-recovery of prudently incurred costs. As in the case of new municipal systems that use the transmission system of their retail customers' former supplier, such costs would not be stranded but for the action of this Commission in requiring a utility to make unbundled transmission services available. [FN690]

Just as we will not be the primary forum for stranded cost recovery for all new municipalizations, so also we will not be the primary forum for stranded cost recovery for all cases of municipal annexation. Instead, our holding is limited to those cases in which the existing municipal system uses Commission-mandated transmission access from the annexed customers' former supplying utility to obtain power from a new supplier. Costs that are exposed to nonrecovery when an existing municipal utility does not use the transmission system of the retail customers' former supplier to reach a new generation supplier (e.g., through self-generation or use of another utility's transmission system) do not meet the definition of "wholesale stranded costs" for which the Rule provides an opportunity for recovery. Such costs are outside the scope of the Rule because such costs would not be stranded as a direct result of Commission-required transmission access. ***12409**

We reject as misplaced the argument that the Commission, by failing to address costs that arise if a municipal utility (whether a new municipal utility or an existing municipal utility that annexes additional retail customer territory) does not use the historical supplying utility's transmission system, has not met its statutory obligation to "set just and reasonable" rates. The Commission in this rulemaking has not determined any utility's just and reasonable rates. Further, Order No. 888 does not by its terms bar the recovery of costs that do not result from the use of Commission-required transmission access. Utilities may, as before, seek recovery of such non-open access-related costs on a case-by-case basis in individual rate proceedings. The Commission will not prejudge those issues here.

As we indicated in Order No. 888, we also are concerned that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission—either this Commission or state commissions—to address recovery of stranded costs.[FN691] We reiterate that we reserve the right to address such situations on a case-by-case basis.

We share the concern expressed by Puget that a retail-turned-wholesale customer should not be allowed to avoid any stranded cost obligation that it may have under Order No. 888 simply by having its new supplier be the entity that requests and contracts for transmission service from the former supplying utility. We clarify that the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers under Order No. 888 applies if the transmission system of the former supplier is used to transmit the newly obtained power supplies to the departing retail customer, regardless of whether the customer or its new supplier is the actual entity that requests and contracts for the unbundled transmission service. We have revised the definition of "wholesale stranded cost" in section 35.26(b)(1)(ii) accordingly to include the situation in which the retail customer subsequently becomes, either directly or through another wholesale transmission purchaser, an unbundled wholesale transmission services customer of the former supplying utility.

We clarify in response to SoCal Edison's request that our decision to be the primary forum for recovery of stranded costs from retail-turned-wholesale customers is not intended to prevent or to interfere with the authority of a state to permit any recovery from departing retail customers, such as by imposing an exit fee prior to creating the wholesale entity. As we indicated in Order No. 888, if the state has permitted any such recovery from a departing retail-turned-wholesale customer, that amount will not in fact be stranded. Accordingly, we will deduct that amount from the costs for which the utility will be allowed to seek recovery from this Commission.[FN692]

We clarify in response to SoCal Edison's request that the Commission has the discretion to defer to a state stranded cost calculation methodology. However, because we recognize that state retail access plans may present questions that need to be addressed on a case-by-case basis, we will consider whether to exercise that discretion on a case-by-case basis.

7. Recovery of Stranded Costs Caused by Retail Wheeling

In Order No. 888, we concluded that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in order to reach a different generation supplier, and that utilities are entitled, from both a legal and a policy perspective, to an opportunity to recover all of their prudently incurred costs.[FN693] We explained that this Commission's authority to address retail stranded costs (i.e., stranded costs associated with retail wheeling customers) is based on our jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, and that the authority of state commissions to address retail stranded costs is based on their jurisdiction over local distribution facilities and the service of delivering electric energy to end users. Because it is a state decision to permit or to require the retail wheeling that causes stranded costs to occur, we decided we generally will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority[FN694] does not have authority under state law to address stranded costs when the retail wheeling is required. In such a case, we will permit a utility to seek a customer-specific surcharge to be added to an unbundled transmission rate.

We noted that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We indicated that rates for services using facilities used in local distribution to make a retail sale are state-jurisdictional, and that states will be free to impose stranded costs caused by retail wheeling on facilities or services used in local distribution. We also said that states may use their jurisdiction over local distribution facilities or services to recover so-called stranded benefits.

We stated that we believe our approach to stranded costs associated with retail wheeling customers represents an appropriate balance between federal and state interests that ensures that the rates for transmission in interstate commerce by public utilities (except in a narrow circumstance) will not be burdened by retail costs.

We expressed concern about the cost-shifting potential in a holding company or other multi-state situation, where denial of retail stranded cost recovery by a state regulatory authority could, through operation of the reserve equalization formula in a Commission-jurisdictional intra-system agreement, inappropriately shift the disallowed costs to affiliated operating companies in other states. We said that we will deal with such situations if they arise pursuant to public utility filings under section 205 or complaints under section 206. Thus, the need to amend a jurisdictional agreement to prevent stranded costs associated with retail wheeling customers from being shifted to customers in other states will be addressed on a case-by-case basis. We encouraged the affected state commissions in such situations to seek a mutually agreeable approach to this potential problem. If such a consensus solution resulted in a filing to modify a jurisdictional agreement, we indicated that we would accord such a proposal deference, particularly if other interested parties support the filing. In the event that the state commissions and other interested parties cannot reach consensus that would prevent cost shifting, we said that the Commission would ultimately have to resolve the ***12410** appropriate treatment of such stranded costs.

Rehearing Requests Opposing Any Commission Involvement in Stranded Costs Associated With Retail Wheeling Customers

A number of entities dispute the Commission's statement that both it and the states have the legal authority to address stranded costs that result from retail wheeling. Central Illinois Light contends that the Commission's claim of dual jurisdiction is inconsistent with FPC v. Southern California Edison Company.[FN695] It says that the court in that case recognized that Congress meant to draw a bright line easily ascertained between state and federal jurisdiction, making unnecessary case-by-case analysis. Central Illinois Light asserts that the Commission has stepped over the bright line into the states' exclusive jurisdiction over retail rates.

IA Com seeks rehearing of the Commission's assertion of concurrent jurisdiction with state authorities over stranded costs associated with retail wheeling customers on the ground that it is based on the Commission's erroneous assertion of jurisdiction over unbundled retail transmission.

IL Com says that regardless of whether the Commission's claim of jurisdiction over retail transmission is upheld, the Commission's ruling that there is joint jurisdiction over retail stranded costs is in error. According to IL Com, the Commission has no authority over such stranded costs. IL Com also disputes the Commission's characterization of the derivation of state authority to address such stranded costs. It says that state commission authority does not derive only from states' jurisdiction over local distribution facilities and the service of delivering electric energy to end users. IL Com submits that state commission authority to address retail stranded costs derives from the existence of state commission jurisdiction over the facilities and costs at the time of their incurrence.

A number of entities contend that Commission jurisdiction over transmission facilities used in interstate commerce does not give it jurisdiction over stranded investment in retail generating assets.[FN696] Several argue that the fact that a retail wheeling customer might need transmission access from its former supplier does not change the character of the costs that are stranded. They maintain that retail stranded costs are not costs of providing unbundled transmission service, but are costs associated with providing what was formerly bundled retail service, over which the Commission has no jurisdiction.[FN697]

Several entities argue that it is solely the action of the state that allows a given utility's retail customers to seek alternative sources of supply; therefore, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime.[FN698]

A number of entities submit that the provision of FPA section 201 that federal regulation is "to extend only to those matters which are not subject to regulation by the States" bars any attempt by the Commission to displace or supplant an admittedly legitimate exercise of state authority over retail stranded costs.[FN699] NASUCA submits that all state commissions have the authority to establish just and reasonable rates for the retail electric utilities in their respective jurisdictions.[FN700] It maintains that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws; the Commission has no knowledge or expertise regarding the specific state legal frameworks in which these costs were included in rates. NY Com argues that the Commission does not have jurisdiction to determine the rate treatment of costs devoted to retail service and, thus, lacks authority to allow recovery if a state decides not to do so.

VA Com argues that section 201(b)(1) of the FPA restricts the Commission's jurisdiction to wholesale sales. It says that a departing retail customer remains a retail customer, regardless of the supplier. VA Com concludes that no portion of the transaction is a wholesale sale, and that there are no wholesale costs associated with a retail wheeling transaction.[FN701]

A number of entities seek rehearing of the Commission's decision that it will entertain stranded cost claims when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required. [FN702] NARUC submits that Congress did not intend the Commission to become involved in adjudicating legal questions regarding the breadth of state law authority granted state commissions by their legislatures. NARUC expresses concern that the Commission would second-guess a state cost recovery determination and promote forum shopping. Once a balance has been struck at the state level concerning the terms of restructuring, NARUC submits that it is inconceivable that the Commission would have either the desire or authority to second-guess a state's legislative and regulatory processes.

Several entities object that the Commission effectively would authorize recovery of stranded costs associated with a retail wheeling customer if a state legislature withholds from the state regulatory agency the authority to approve stranded cost recovery.[FN703] They submit that just because a state has not given its regulatory commission the authority to impose stranded costs in the case of retail wheeling does not confer jurisdiction on the Commission to impose such charges. They contend that the state legislature should be the final arbiter of state policy. IL Com submits that if a state legislature chooses not to give its state commission the authority to act on stranded costs, "that can be taken as a clear indication that the state's legislature most certainly does not want FERC to address them."[FN704] Central Illinois Light objects that the Commission has offered no reason why it will accept the decision ***12411** of the regulatory agency, but not that of the legislature.

AMP-Ohio and Cleveland ask the Commission to clarify that its deference to the determinations of the states is to the authority of the states as exercised through state legislative bodies (and other political subdivisions with legislative authority) as well as to state regulatory bodies. They submit that if the state legislature, or a local government acting in accordance with its authority, enacts retail wheeling legislation that expressly limits the ability of its regulatory body to permit recovery of stranded costs, even barring all such recovery, the Commission should not become involved.

Several entities ask the Commission to clarify that Order No. 888 does not permit utilities to apply to the Commission for recovery of stranded costs associated with a retail wheeling customer when a state regulatory authority has "addressed" a request for the same stranded costs but has not allowed 100 percent recovery.[FN705] ELCON gives two hypothetical examples to which it asks the Commission to respond: one where a state regulatory authority possesses full stranded cost recovery authority but allows only 50 percent recovery; the other where the state legislature provides the state regulatory authority by statute with the power to permit recovery of up to 50 percent of identified stranded costs.

Commission Conclusion

We reaffirm our conclusion that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in interstate commerce from public utilities in order to reach a different generation supplier, but that, because it is a state decision to permit or require the retail wheeling that causes retail stranded costs to occur, we will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required.

We will reject the requests for rehearing that oppose any Commission involvement in stranded costs associated with retail wheeling customers. We disagree with those entities that challenge our conclusion that both this Commission and the states have the legal authority to address stranded costs that result from retail wheeling (variously described by those entities as dual, concurrent, or joint jurisdiction). The Commission explained in detail in Order No. 888 the legal basis for concluding that this Commission and the state commissions each have jurisdiction over separate aspects of a retail wheeling transaction.[FN706] This Commission has jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities. State commissions have jurisdiction over local distribution facilities and the service of delivering electric energy to end users. Based on our respective jurisdictions over separate aspects of the retail wheeling transaction, we believe either has the authority to provide the former supplying utility with an opportunity to recover costs stranded when the departing customer uses retail transmission in interstate commerce to reach a new supplier, but that here, unlike the retail-turned-wholesale scenario, the state commission should be the primary forum because these costs are stranded by the action of the state. We would act only if the primary forum is not available. We have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity to seek recovery of prudently incurred costs.

Several entities argue that the Commission does not have jurisdiction over stranded investment in retail generating assets, that use of Commission-jurisdictional transmission does not change the character of the costs that are stranded, that stranded costs associated with retail wheeling customers are not costs of providing unbundled transmission service, but are costs associated with providing what was formerly bundled retail service, and that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws. While we agree that stranded costs associated with retail wheeling are costs that are retail in character in the sense that they are in retail bundled rates and become stranded as a result of retail wheeling required by the state commission, we do not believe this precludes the Commission from exercising jurisdiction in the limited circumstances of the Rule.

As an initial matter, we note that there are rarely separate retail and wholesale generating facilities. Retail customers and wholesale requirements customers get energy from the same facilities, each buying a "slice of the system." Typically all generating assets go into both the retail and the wholesale rate bases for determining retail and wholesale rates. Rates are determined by allocating the total generating costs among customer classes. The parties confuse the issue before us to the extent they suggest that state commissions, not this Commission, have "jurisdiction" over certain "costs." Neither the state commissions nor this Commission has exclusive jurisdiction over "costs." Each regulatory authority has jurisdiction to determine "rates" for services subject to its jurisdiction and, in determining rates, may take into account all of the costs incurred by the utility. Under historical cost-of-service ratemaking, each regulatory authority, in exercising its respective ratemaking jurisdiction, reviews the total costs incurred by a utility to provide service and makes its separate and independent determination of what costs may be recovered through rates within its jurisdiction.[FN707] Generating costs continually shift between retail and wholesale rates over time.[FN708]

More importantly, both the state commission and this Commission have a responsibility to oversee the financial health of the utilities we regulate. Each has jurisdiction to make judgments about recovery of the costs of the assets in the utility's total rate base. Utilities are entitled to a regulatory forum that can adjudicate claims that they are or are not entitled to recovery of costs incurred regardless of the initial retail or wholesale "character" of those costs, and we believe we have the authority and obligation to fill a regulatory "gap" that could occur.[FN709]

In response to the argument that it is solely the action of the state that allows a retail customer to seek alternative sources of supply and, as a result, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime, we agree. Indeed, as we indicate in Order No. 888, we decided to leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling (with a limited exception) because it is a state decision to permit or require the retail wheeling in the first instance that causes retail stranded costs to occur. Our determination, as explained above, is to fill any regulatory gap that arises as a result of interstate wheeling. We believe that it is necessary for the Commission to act as a backstop in this limited instance to ensure that costs stranded as a result of retail wheeling do not go unrecovered because the state regulatory authority lacks the authority under state law to address such costs. At the same time, as we stated in Order No. 888, we believe that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We emphasize that this Rule is not intended to preempt the exercise of any existing state authority with respect to the assessment of a stranded cost or stranded benefits charge on a retail customer that obtains retail wheeling.

In response to arguments that the Commission's decision will result in second-guessing or interfering with a state's legislative processes and decisions, we believe these arguments are premature. As a general matter, we do not expect that our decision to be a backstop will interfere with legislative decisions that specifically address stranded cost matters and the scope of the state regulatory authority's authority in determining stranded costs. If states or parties to a retail stranded cost recovery case brought before this Commission believe that a Commission decision on the issue would interfere with state legislative decisions, they should raise their arguments, and support therefore, at that time.

We clarify that Order No. 888 does not permit utilities to seek recovery from the Commission of stranded costs associated with retail wheeling customers if a state regulatory authority with authority to address retail wheeling stranded costs has in fact addressed such costs, regardless of whether the state regulatory authority has allowed full recovery, partial recovery, or no recovery.

Rehearing Requests Supporting Broader Jurisdiction Over Stranded Costs Associated With Retail Wheeling Customers
A number of entities seek rehearing of the Commission's decision not to serve as a backstop for all stranded costs associated with retail wheeling customers. Some assert that the Commission has the legal authority to address independently stranded

costs that arise from retail wheeling and that the Commission cannot lawfully abdicate or delegate such authority to the states.[FN710] Coalition for Economic Competition submits that the Commission correctly concluded that it has jurisdiction over retail transmission rates, terms and conditions and the authority to address retail wheeling stranded costs. Thus, it argues that the Commission is without the power to make a "policy determination" that results in the Commission not exercising its legal authority over stranded costs associated with retail wheeling customers. It asserts that, just as the Commission recognizes that it "cannot simply turn over its jurisdiction" to the states to determine facilities subject to Commission jurisdiction,[FN711] the Commission cannot turn over its jurisdiction to establish stranded cost charges that it correctly determined it has the authority to establish. Coalition for Economic Competition argues that the Commission should adopt a stranded cost recovery policy similar to the policy the Commission has adopted with respect to the determination of state/federal jurisdiction, whereby the Commission would defer to state stranded cost determinations so long as they are consistent with the Commission's policy.

Utilities For Improved Transition argues that the Commission's authority over public utility rates for the transmission of electric power, both wholesale and retail, is plenary and exclusive. As a result, it submits that the Commission may not avoid responsibility for costs stranded by transmission of retail power.[FN712] Illinois Power contends that Congress did not authorize the Commission to reject jurisdictional rate filings whenever the Commission regards the state commissions as a more convenient or appropriate forum.

EEI and the Coalition for Economic Competition contend that virtually all retail stranded costs can only occur through the vehicle of Commission-jurisdictional transmission in interstate commerce. They submit that the Commission, having recognized the clear nexus between FERC-jurisdictional transmission and stranded costs in the retail-turned-wholesale context, cannot fail to recognize the same clear nexus in the retail wheeling context.

Utilities For Improved Transition says that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states' doing so; the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service.

Coalition for Economic Competition and Utilities For Improved Transition contend that the Commission must consider stranded costs that arise from retail wheeling in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. Coalition for Economic Competition maintains that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (e.g., wholesale wheeling and new municipalizations) but to exclude them from other jurisdictional wheeling rates (e.g., retail wheeling, municipal ***12413** annexation, and bypass).[FN713] Utilities For Improved Transition says that the just and reasonable standard requires the Commission to backstop the states to ensure that there is full stranded cost recovery. It objects that Order No. 888's disposition of jurisdiction creates a problem of cross-class discrimination (wholesale versus retail) and inter-class discrimination (some retail versus the remainder of the retail).

Coalition for Economic Competition further argues that the Commission's failure to address all stranded costs associated with retail wheeling customers will result in an improper taking under the Constitution.[FN714] It also argues that the Commission is not permitted to disregard its findings in Order No. 888 which, according to Coalition for Economic Competition, "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail wheeling, municipal annexation, and bypass stranded costs) is required.[FN715]

Illinois Power argues that the FPA does not authorize the Commission to discriminate among utilities based on the state of their residence, and that the Commission must allow all utilities to seek interstate rate recovery of just and reasonable retail stranded costs. Illinois Power asserts that the Rule will lead to the absurd, unduly discriminatory result that utilities located in states whose legislatures have failed to provide for stranded cost recovery will be better off than those located in states that provide for only limited stranded cost recovery. It supports use of the Commission's statutory authority to establish a uniform, national method for retail stranded cost recovery.

Coalition for Economic Competition also contends that the Commission's decision to let the states deal with retail stranded costs is arbitrary and capricious because the Commission failed to consider the arguments that stranded cost opponents will make before state commissions, such as that a state lacks jurisdiction to impose stranded cost charges or that the state imposition of such charges may be preempted or found to be an undue burden on interstate commerce. It further argues that the Commission's reliance on state jurisdiction over the service of delivering electric energy to the end user does not reflect reasoned decisionmaking. It submits that the Commission has failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, in which case the state commission may have no jurisdiction over either the sale or the transmission of the energy and, accordingly, no authority to consider stranded costs.

A number of entities ask the Commission to act on requests for retail stranded cost recovery when the state commission lacks authority or has authority to order recovery, but has declined to do so or has only allowed partial recovery.[FN716]

Lastly, TX Com notes that section 35.26(d) (dealing with recovery of retail stranded costs) refers only to public utilities. It suggests that the omission of a reference to transmitting utilities appears to be inadvertent and should be corrected.

Commission Conclusion

The Commission will reject the requests for rehearing of our decision not to assume a backstop role for all stranded costs associated with retail wheeling customers. We explained in Order No. 888 that commenters that describe our action as an unlawful abdication or delegation of authority misconstrue the nature of our decision to leave stranded costs associated with retail wheeling customers (with a limited exception) to state regulatory authorities.[FN717] We have not "abdicated" or "delegated" to state regulatory authorities our jurisdiction over the rates, terms, and conditions of retail transmission in interstate commerce; if retail transmission in interstate commerce by a public utility occurs, public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.[FN718] Instead, we have made a policy determination that the recovery of stranded costs associated with retail wheeling customers—an issue over which either this Commission or state commissions could exercise authority by virtue of their jurisdiction over retail transmission in interstate commerce and over local distribution facilities and services, respectively—is primarily a matter of local or state concern for which the primary forum should be the state commissions. However, if the state regulatory authority does not have authority under state law to be the forum to address stranded costs when the retail wheeling is required, then we will entertain requests to recover such costs. As we explain above in response to the rehearing petitioners that oppose any Commission involvement in stranded costs associated with retail wheeling customers, we have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity to seek recovery of prudently incurred costs.[FN719]

We disagree with Coalition for Economic Competition's argument that our findings in Order No. 888 "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail wheeling and bypass stranded costs) is required, much less that the Commission has ignored the findings in Order No. 888. To the contrary, as we explain in Section IV.J.1, it is not the purpose of this Rule to allow utilities an opportunity to seek to recover "all" uneconomic costs that might be stranded when a customer leaves its utility supplier. We have fully explained our reasons for adopting an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of stranded cost recovery from retail customers, recognizes state commission jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures. ***12414**

We disagree with those entities that contend that the Commission must consider retail stranded costs in order to satisfy our statutory obligation under the FPA to set just and reasonable rates. In determining just and reasonable rates for jurisdictional transmission service, which currently are determined on a cost basis, the Commission satisfies its statutory obligation under the FPA by allowing utilities an opportunity to recover their prudently incurred costs plus a reasonable rate of return. As we have explained above, this may include the costs of use of the physical transmission system, as well as economic costs incurred by the utility when it provides transmission service (e.g., stranded costs). However, in situations in which a state regulatory authority has the authority to address recovery of retail stranded costs, there is no regulatory "gap," and there is no obligation for this Commission to provide a second opportunity for recovery.[FN720]

We reject arguments that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (wholesale wheeling and new municipalizations) but to exclude them from other jurisdictional wheeling rates (retail wheeling in interstate commerce and use of another utility's transmission tariff), and that this policy somehow makes rates discriminatory. Recovery of this type of cost through a transmission rate is obviously not the norm, but is necessitated by the need to deal with the transition costs associated with this Rule. As discussed in detail in the Rule, the Commission has carefully balanced the interests of utilities as well as customers in concluding that the opportunity for stranded cost recovery through transmission rates should be permitted in only two general circumstances: (1) in the case of wholesale stranded costs, where there is a direct nexus to Commission-required transmission access; and (2) in the case of retail stranded costs, where there otherwise would be a regulatory gap because a state regulatory authority lacks authority under state law to address stranded costs at the time that retail wheeling is required. We see nothing in the FPA that precludes us from exercising this flexibility and, indeed, the parties have not pointed to anything that, in our opinion, precludes us from exercising this discretion.

We reject the argument that virtually all stranded costs associated with retail wheeling customers can occur only through the vehicle of Commission-jurisdictional transmission in interstate commerce, and therefore, that the same nexus between FERC-jurisdictional transmission and stranded costs that exists in the retail-turned-wholesale context is present in the retail wheeling context. We also disagree that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states doing so, and that the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service. The opportunity for stranded cost recovery set forth in this Rule is based on the causal link between stranded costs and the availability and use of the Commission-required transmission tariff. It is true that in both the retail-turned-wholesale context and the retail wheeling context there is a limited nexus between stranded costs and Commission-jurisdictional access since, in both situations, the Commission has jurisdiction over the rates, terms and conditions of the transmission service and, therefore, the authority to permit stranded cost recovery through the transmission rates. However, the causal nexus to FERC-jurisdictional transmission and stranded costs in the two contexts (retail vs. retail-turned-wholesale) is different. In the retail wheeling context, there is no causal nexus between stranded costs and transmission that has been ordered by this Commission. In the retail-turned-wholesale context, in contrast, the opportunity for a utility to seek recovery of stranded costs is grounded on the existence of a direct causal nexus between stranded costs and transmission that has been ordered by this Commission.

We will reject the rehearing petitions that ask the Commission to act on requests for stranded cost recovery associated with retail wheeling customers not only when the state commission lacks authority, but also when the state commission has authority but either has declined to use it or has only allowed partial recovery. As explained above, our decision to entertain requests to recover stranded costs caused by retail wheeling in a limited circumstance (when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on our determination to fill any regulatory gap that arises in association with interstate transmission.

We will reject TX Com's request that the Commission clarify that section 35.26(d) (dealing with recovery of retail stranded costs), which refers only to public utilities, should also refer to transmitting utilities. The Commission's decision to act as a limited backstop in the case of stranded costs associated with retail wheeling customers is based on our jurisdiction under sections 205 and 206 of the FPA over the rates, terms, and conditions of retail transmission in interstate commerce. As a result, our ability to allow the recovery of such costs through a surcharge on a section 205 unbundled transmission rate is necessarily limited to public utilities.[FN721]

Rehearing Requests Opposing Commission Treatment of Stranded Costs Associated With Retail Wheeling Customers in Holding Company Intra-System Agreement Cases

A number of entities oppose the Commission's proposal to address on a case-by-case basis whether jurisdictional intra-system agreements may need to be amended in order to prevent inappropriate cost-shifting that could occur if one state disallows stranded cost recovery associated with retail wheeling customers. IN Com objects that the problem is not the actions of one state or another, but rather the terms of the intra-system agreement.

AR Com objects that Order No. 888 is factually in error because a state's treatment of retail stranded costs under the Entergy System Agreement cannot shift costs to other jurisdictions.[FN722] It submits that whenever retail load changes, whether due to retail wheeling or any other factor, responsibility ratios under Entergy's reserve equalization schedule, MSS-1, will change and costs will shift irrespective of the regulator's treatment of retail stranded costs. AR Com says that MSS-1 reveals no changes in calculations due to retail treatment of stranded costs or any other retail ratemaking; only “excess” capacity costs of intermediate gas- and oil-fired plant are “shifted” under the Entergy System Agreement. Although the Commission has the authority to amend intra-system agreements when ***12415** wholesale cost allocations have become unjust and unreasonable, AR Com submits that the Commission does not have jurisdiction to reach to the state level and dictate what retail ratepayers should pay to shareholders. AR Com maintains that a FERC-jurisdictional intra-system agreement extends only to sales for resale (transactions among subsidiaries), and that if a holding company believes that an intra-system agreement is unduly discriminatory as a result of a state's disallowance of costs, the holding company can propose to amend it.[FN723]

AR Com argues that retail stranded costs fall to state jurisdiction regardless of whether the utility is a member of an interstate holding company. AR Com says that because the costs at issue are in retail rate base, any Commission influence over their recovery could occur only through preemption, but preemption of a state disallowance from retail rate base is possible only if there is a “trapped cost.” AR Com submits that a disallowance of retail rate base cost cannot result in a trapped cost because there is no inconsistency between two agencies acting within their jurisdiction; the Commission has no jurisdiction to act. AR Com maintains that, unlike the Grand Gulf situation, the Commission has not mandated any Entergy generation costs into retail rate base. It further says that different state decisions regarding recovery of retail costs are not inconsistent decisions; they represent each state applying its law to its facts. According to AR Com, decisions by states leading to less than full recovery could be deemed inconsistent decisions only if there were a federal guarantee of full cost recovery of retail costs, which there is not.

AR Com and MO/KS Coms assert that the Commission's proposal for holding company situations cannot apply to future holding companies, where there is no history of joint planning justifying cost equalization, nor can it apply to future investments. They contend that this would require an assumption that the utility subsidiaries of a registered holding company have planned, and should plan, together rather than separately (i.e., that interaffiliate transactions are always more efficient than nonaffiliate transactions), and that such assumption would be sound only if having the transaction occur between affiliates is inherently more efficient than having the transaction occur between an affiliate and a nonaffiliate.

Commission Conclusion

The comments raised for the most part are either premature or reflect a misunderstanding of the Commission's decision. Contrary to AR Com's argument, the Commission in Order No. 888 in no way asserted jurisdiction over state determinations of stranded costs associated with retail wheeling customers. We agree with AR Com that our jurisdiction extends only to sales for resale (and transmission in interstate commerce) and that a holding company can seek to amend an intra-system agreement if it believes the agreement is unduly discriminatory as a result of a state's disallowance of costs. However, a holding company also may seek to amend an agreement before any potential disallowances can occur, to keep cost-shifting from occurring. The fact is that intra-system agreements which involve wholesale sales among affiliate companies in different states could, through operation of their reserve equalization formulas, result in customers in one or more states having to indirectly bear stranded costs that are disallowed in another state, and the Commission has a responsibility to prevent inappropriate cost-shifting. Such determinations can be made only on a case-by-case basis. Again, as we stated in Order No. 888, we encourage affected state commissions to propose mutually agreeable solutions to this potential problem.

8. Evidentiary Demonstration Necessary—Reasonable Expectation Standard

In Order No. 888, the Commission concluded that a utility seeking to recover stranded costs must demonstrate that it had a reasonable expectation of continuing to serve a customer. We stated that whether a utility had a reasonable expectation of continuing to serve a customer, and for how long, will be determined on a case-by-case basis, and will depend on all of the facts and circumstances. We also determined that the existence of a notice provision in a contract would create a rebuttable presumption that the utility had no reasonable expectation of serving the customer beyond the specified period. We said that whether or not a contract contains an "evergreen" or other automatic renewal provision will be a factor to be considered in determining whether the presumption of no reasonable expectation is rebutted in a particular case.[FN724]

We also said that we would apply the reasonable expectation standard to retail-turned-wholesale customers. We explained that, before the Commission will permit a utility to recover stranded costs, the utility must demonstrate that it incurred such costs based on a reasonable expectation that the retail-turned-wholesale customer would continue to receive bundled retail service. Whether the state law awards exclusive service territories and imposes a mandatory obligation to serve would be among the factors to be considered in determining whether the reasonable expectation test is met in a particular case.[FN725]

We noted that Order No. 888 does not address who will bear the stranded costs caused by a departing generation customer if the Commission finds that the utility had no reasonable expectation of continuing to serve that customer. We indicated that we anticipate that, in such a case, a public utility will seek in subsequent requirements rate cases to have the costs reallocated among the remaining customers on its system. However, we stated that we were not prejudging that issue in the Rule.[FN726]

Rehearing Requests Opposing or Seeking Modification of the Reasonable Expectation Standard

APPA challenges the reasonable expectation standard as being too vague. It submits that the Commission has provided no guidance concerning application of the reasonable expectation standard, other than to state that it would decide the issue on a case-by-case basis. APPA objects that public utilities can exploit the uncertainty created by this standard, which will lead to costly and time-consuming litigation. IL Com supports replacing the reasonable expectation standard with a statutory, regulatory, contractual standard.

Several entities contend that there is no basis to conclude that the reasonable expectation test could ever be met. VT DPS and Valero submit that, since 1973, utilities have known that a refusal to wheel power could subject them to antitrust liability. They say that Order No. 888 ignores the breadth of NRC ***12416** licensing conditions. LEPA similarly argues that the reasonable expectation standard could not be met where NRC license conditions required an explicit wheeling commitment and prohibited the utility from including in the wheeling cost any amount attributable to the loss of customers due to the wheeling. It objects that delaying a decision on stranded cost recovery in such cases holds the threat of possible stranded cost charges over the heads of bulk power purchasers and thereby chills their ability to seek competitive sellers.

TAPS asserts that there should be an irrefutable presumption that no stranded costs are due from customers with pre-existing transmission rights, including customers who were the beneficiaries of NRC license conditions.[FN727] TAPS submits that there can be no legitimate "reasonable expectation" that such customers would continue to purchase power if the price was higher than the market price.

Occidental Chemical asks the Commission to clarify that a utility could have had no reasonable expectation of recovering stranded costs from customers who, prior to the issuance of the NOPR, had the opportunity to switch to an alternative electric supplier or had the option of self-generating, obtaining on-site third-party generation, or municipalizing. Occidental Chemical further argues that it defies commercial expectations to allow a utility to argue that if a contract is silent on the issue of renewal, the obligation to purchase does not expire with the termination of the contract. It submits that the Commission has not shown that it has the authority to force customers to extend purchase agreements against their will in violation of accepted commercial practice.

A number of entities submit that the Commission erred in failing to treat a notice of termination provision as conclusive evidence that the utility had no reasonable expectation of continued service.[FN728] Several object that the Commission has failed to explain why the presence of a notice provision does not conclusively demonstrate the lack of a reasonable expectation and ipso facto terminate the obligation of the customer to purchase the product.[FN729] APPA objects that the Commission provided no evidence that it considered comments supporting making the presumption conclusive and that it found legally sufficient reasons to reject them.

PA Munis objects that the rebuttable presumption represents an unjustified departure from the Commission's traditional policy of enforcing the express terms of notice provisions without any inquiry into the reasonable expectations of the party, provided that the agreements were negotiated in good faith and approved by the Commission.[FN730] PA Munis contends that wholesale requirements customers negotiated notice provisions with the knowledge that the Commission would enforce the notice provisions according to their terms, including the specific length of the term. [FN731] PA Munis argues that it is arbitrary and capricious to provide utilities an opportunity to seek to amend these contracts.

Several entities submit that the rebuttable presumption invites litigation and promotes uncertainty for customers.[FN732] APPA objects that the Commission has failed to establish the showing that it would require to overcome the presumption.

Referring to the Commission's discussion of evergreen provisions, Central Montana EC argues that it is wrong to infer from the existence of an automatic renewal provision that the parties intended that the contract might run longer than its initial term. Central Montana EC asserts that the presence of an evergreen provision infers simply that the parties agreed upon a mechanism to avoid the renegotiation of a power supply contract if, at the conclusion of its initial term, the parties were satisfied with the contract. It maintains that the parties' obligations are defined by the term and termination provisions of wholesale power contracts, and that the presence of a mechanism to avoid contract renegotiation does not alter those termination rights.

Commission Conclusion

We will reject the requests for rehearing of our decision to adopt a reasonable expectation standard to be applied on a case-by-case basis and to treat a notice provision in a contract as a rebuttable, not a conclusive, presumption of no reasonable expectation. Contrary to the claims of some entities, the Commission has explained the basis for its finding that utilities may have had an implicit obligation to serve their wholesale requirements customers and, therefore, that a utility should be given an opportunity to demonstrate that it incurred costs to provide service to a customer and that it had a reasonable expectation that it would continue to serve the customer beyond the contract termination date. The same factors that some petitioners contend establish the absence of a reasonable expectation of continued service may be offered as evidence to be considered in determining whether the reasonable expectation test is met in a particular case.

We believe that our decision to treat a notice of termination provision in a contract as creating a rebuttable presumption that the utility had no reasonable expectation of serving the customer beyond the period provided for in the notice provision is a reasonable one. It places evidentiary significance on the fact that a contract contains a notice of termination provision. Moreover, while it gives the utility an opportunity, based on the facts and circumstances of a particular case, to rebut the presumption of no reasonable expectation, it firmly places the burden of establishing reasonable expectation on the utility. Although some entities support treating notice provisions as a conclusive presumption of no reasonable expectation, as discussed below, we decline to adopt such an inflexible approach. Nevertheless, as we indicated in Order No. 888, when a utility is seeking a contract amendment to permit stranded cost recovery based on expectations beyond the stated term of the contract, we believe that the utility has a heavy burden in demonstrating that the contract ought to be modified.[FN733]

Contrary to the position of PA Munis, the rebuttable presumption is fully consistent with the Commission's past treatment of notice provisions. For example, the Kentucky Utilities Company case cited by PA Munis supports the proposition that, until a customer exercises a notice of ***12417** termination provision, the utility is under an implicit obligation to continue to serve and plan for the future needs of the customer.[FN734] Thus, the presence of a notice of termination provision in a contract (particularly one not yet exercised by the customer), in and of itself, may not necessarily support the conclusion that the utility could never prove that it reasonably expected to continue serving the customer beyond the notice period.[FN735]