

ORAL ARGUMENT SCHEDULED FOR MARCH 8, 2004

**IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT**

No. 03-1162

**CONSUMERS ENERGY COMPANY,
PETITIONER,**

v.

**FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.**

**ON PETITION FOR REVIEW OF ORDERS OF THE
FEDERAL ENERGY REGULATORY COMMISSION**

**BRIEF OF RESPONDENT
FEDERAL ENERGY REGULATORY COMMISSION**

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JANUARY 9, 2004

CIRCUIT RULE 28(a)(1) CERTIFICATE

A. Parties and Amici

The parties before this Court are identified in the brief of Petitioner.

B. Rulings Under Review

1. *Ontario Energy Trading International Corp.*, 99 FERC ¶ 61,039 (2002);
2. *Ontario Energy Trading International Corp.*, 100 FERC ¶ 61,345 (2002); and
3. *Ontario Energy Trading International Corp.*, 103 FERC ¶ 61,044 (2003).

C. Related Cases

This case has not previously been before this Court or any other court. Counsel is not aware of any other related cases pending before this or any other court.

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January 9, 2004

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GLOSSARY

April 2003 Order	<i>Ontario Energy Trading International Corp.</i> , 103 FERC ¶ 61,044 (2003)
FERC	Federal Energy Regulatory Commission
FTR	financial transmission right
IMO	Ontario Independent Electricity Market Operator
Initial Order	<i>Ontario Energy Trading International Corp.</i> , 99 FERC ¶ 61,039 (2002)
IZP	intertie zone price
Midwest ISO	Midwest Independent Transmission System Operator
New York ISO	New York Independent Transmission System Operator
Ontario	Ontario Energy Trading International Corporation
OPG	Ontario Power Generation, Inc.
PJM	PJM Interconnection, Inc.
RTO	regional transmission organization
September 2002 Order	<i>Ontario Energy Trading International Corp.</i> , 100 FERC ¶ 61,345 (2002)
SMD Order	<i>Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design</i> , 100 FERC ¶61,138 (2002)

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**BRIEF OF RESPONDENT
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STATEMENT OF THE ISSUE

Whether the Commission reasonably granted Ontario's market-based rate application upon finding that Ontario's Canadian affiliate's market power was adequately mitigated where the affiliate was required by statute to maintain a tariff ensuring nondiscriminatory open access transmission, the affiliate provided service comparable to that available to Ontario in the United States, and there was no evidence to support allegations of discriminatory conduct.

STATUTORY AND REGULATORY PROVISIONS

The pertinent statutes and regulations are contained in the Addendum to this brief.

STATEMENT OF THE CASE

I. Nature of the Case, Course of Proceedings, and Disposition Below

The challenged orders granted the application of Ontario Energy Trading International Corporation (“Ontario”), a Canadian entity, for authority to sell capacity, energy and ancillary services, and to resell transmission capacity, at market-based rates in the United States. *Ontario Energy Trading International Corp.*, 99 FERC ¶ 61,039 (“Initial Order”), *on reh’g*, 100 FERC ¶ 61,345 (2002) (“September 2002 Order”), *on reh’g*, 103 FERC ¶ 61,044 (2003) (“April 2003 Order”). The Commission allows power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, market power in generation and transmission and cannot erect other barriers to entry. A transmission-owning public utility affiliate demonstrates the absence, or mitigation, of market power by having an open access transmission tariff that offers comparable services. For a Canadian affiliate of a power marketer to provide comparable service, it must offer non-discriminatory wholesale access to its transmission system that can be used by competitors of the power marketer to reach the United States.

Petitioner Consumers Energy Company challenged the Commission’s grant of market-based rate authority to Ontario, contending that Ontario’s affiliate, the Ontario Independent Electricity Market Operator (“IMO”), does not offer open access transmission service on a comparable basis for wheeling through and out of the Province of Ontario. Consumers conceded that the Ontario Electricity Act of 1998 guarantees non-discriminatory access to the IMO’s system, and presented no evidence that the IMO in fact operates its transmission system on a discriminatory basis. Consumers, nonetheless,

contended that the bid-based market operated by the IMO was not comparable to the open access service provided in the United States.

The Commission rejected Consumer's claim, finding that open access was statutorily guaranteed, service was comparable to that provided in the United States, and that no evidence showed Consumers or any other competitor of Ontario has been or will be impeded from reaching United States markets. In fact, at least 12 United States-based wholesale marketing companies have traded successfully in and out of the IMO-administered markets since the IMO began operating on May 1, 2002. Thus, because the IMO provides open access transmission on a comparable, non-discriminatory basis for wheeling through and out of Ontario, Ontario's affiliation with the IMO did not provide a basis for denying Ontario's application for market-based rates.

II. Statement of Facts

A. The Restructuring of the Ontario Power Market

In Order No. 888, the Commission required public utilities to adopt tariffs providing open access to transmission facilities.¹ The Commission also determined that

¹*Promoting Wholesale Competition Through Open Access Nondiscriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, FERC Stats. & Regs. ¶31,036 at 31,760-62 and 31,857, 61 Fed. Reg. 21,540 (1996), *clarified*, 76 FERC ¶61,009 and 76 FERC ¶61,347 (1996), *on reh'g*, Order No. 888-A, FERC Stats. & Regs. ¶31,048, 62 Fed. Reg. 12,274, *clarified*, 79 FERC ¶61,182 (1997), *on reh'g*, Order No. 888-B, 81 FERC ¶61,248, 62 Fed. Reg. 64,688 (1997), *on reh'g*, Order No. 888-C, 82 FERC ¶61,046 (1998), *aff'd sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *cert. denied in pertinent part*, 69 U.S.L.W. 3574 (U.S. Feb. 26, 2001), *aff'd*, *New York et al. v. Federal Energy Regulatory Commission*, 535 U.S. 1 (2002).

otherwise eligible foreign entities should be able to obtain service under a United States public utility's open access tariff. Order No. 888, FERC Stats. & Regs. at 31,689. A foreign entity that owns or controls transmission facilities, however, can take transmission service under a United States public utility's open access tariff only upon compliance with the tariff's reciprocity requirement. *Id.* at 31,761. The reciprocity provision assures that a public utility providing service under its open access tariff to a transmission-owning entity that is not subject to FERC's open access requirement will be able to receive service in turn from that entity. Order No. 888-A, FERC Stats. & Regs. at 30,290.

Ontario Hydro, a government-owned utility that provided generation, transmission, and distribution services in Ontario, sought a stay of the Order No. 888 reciprocity requirement, contending that it would be irreparably harmed by the requirement because it could not allow open access into Ontario without the approval of the Ontario Government, which would require a complete restructuring of the Ontario power system.² Following the Commission's rejection of the request,³ the Ontario legislature enacted the Energy Competition Act of 1998, to break up Ontario Hydro and bring competition to the Ontario electric industry. Application of Ontario Energy Trading International Corp. For Order Approving Market-Based Tariff, R. 1 at 3, JA 9. The

²*Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, 79 FERC ¶61,182 at 61,866 (1997).

³*Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, 79 FERC ¶61,367 (1997).

Electricity Act of 1998, enacted as part of the Energy Competition Act, required the transfer of Ontario Hydro's generation assets to Ontario Power Generation, Inc. ("OPG"), and its transmission assets to Hydro One. *Id.*; Initial Order, 99 FERC at 61,145, JA 87. All shares of both Ontario Power Generation and Hydro One were held in the name of the Provincial Government of Ontario. Initial Order, 99 FERC at 61,145 at n.2, JA 87.

Hydro One then transferred operational control over its transmission assets to the IMO, which is a non-profit, independently-governed transmission and market operator, required by statute to operate its Canadian markets on an open access, non-discriminatory basis, with similar duties and functions to those of a regional transmission organization ("RTO") in the United States. *Id.* at 61,145, JA 87. *See* The Electricity Act of 1998, §§1(b) and 5(1). Ontario, an affiliate of OPG established to buy and sell electricity as a power marketer, owns no power generation or transmission assets. Initial Order, 99 FERC at 61,145, JA 87.

B. Operation of the Restructured Market

The IMO administers a bid-based power market where requests for transmission service are integrated into market participants' energy bids, eliminating the need for a separate transmission reservation mechanism. *See* April 2003 Order, 103 FERC ¶ 61,044 at ¶ 11, JA 1785; Brief of Ontario Energy Trading International Corp., R. 20 at 8-11, JA 129-32. In the internal Ontario market, there are system-wide uniform prices for all energy products, so that all purchases in the IMO market are made at the uniform market-clearing price, plus a uniform uplift constituting payment for the fixed and variable costs of the transmission system, congestion, and other costs. R. 20 at 8, JA 129.

Market participants can export energy out of the Ontario market by bidding to purchase energy from the IMO market at an intertie between Ontario and an adjacent region. R. 20 at 8, JA 129. Energy can be wheeled through Ontario by simultaneously selling into the IMO market at an intertie to import the energy into Ontario, and purchasing energy from the IMO market at an intertie to export the energy. *Id.* In order to make the through transaction firm, the market participant submits a minimum bid to sell into the IMO market at import, and a maximum bid to buy from the IMO market at export. *Id.* at 16, JA 137.

If there is no congestion at either the import or export intertie, both the import and export transactions take place at the uniform IMO market price. *Id.* Thus, the sale and purchase at the uniform IMO price net out, and the only charge for the wheeling transaction through Ontario is an export fee. *Id.*⁴ If there is congestion at an intertie, the IMO sets an intertie zone price (“IZP”) at that intertie, at a level where demand and supply clear the market, subject to applicable transfer limits. *Id.* at 12, JA 133. If the congestion occurs at an export intertie, the IZP would exceed the uniform Ontario price, and therefore a wheeling transaction would be subject to both the export fee and the difference between the uniform IMO price and the IZP price. *Id.* at 16, JA 137.

As with the New York ISO and the PJM Interconnection, Inc. RTO (“PJM”), the IMO manages a market in financial transmission rights (“FTR”) that allow entities

⁴ The export fee is composed of three elements: (a) a pro-rata share of the IMO administrative costs; (b) a pro-rata share of other operating costs, such as internal Ontario congestion management; and (c) a charge of CDN\$1/MWh which covers a portion of the fixed cost of the transmission system. R. 20 at 16, JA 137.

engaging in imports and exports to hedge the risk of incurring congestion costs. *Id.* at 17, JA 138. FTRs, sold in auctions, are purely financial instruments that entitle the holder to payments based on the price difference between the Ontario uniform market-clearing prices and the market clearing prices in the Ontario intertie zones where congestion occurs. *Id.* An FTR holder at a particular intertie is assured of obtaining firm transmission through that intertie at a price that is fixed, *id.*, except for the export fee, which the customer would know prior to engaging in the wheeling transaction. April 2003 Order, 103 FERC at 61,174 n. 11, JA 1785.

C. The Orders Under Review

On February 14, 2002, Ontario filed an application under FPA § 205 seeking authority to sell energy, capacity and ancillary services, and to resell transmission capacity, at market-based rates. Initial Order, 99 FERC at 61,145, JA 87. The Commission allows power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, market power in generation and transmission and cannot erect other barriers to entry. *Id.* at 61,146, JA 88.

In the Initial Order, the Commission found no transmission market power concerns because Ontario did not own or operate transmission facilities, and Ontario was not affiliated with any transmission-owning public utilities. *Id.* at 61,147, JA 89. In particular, the Commission found that the IMO was a not-for-profit corporation that was independent of any market participant, including Ontario. *Id.*

Consumers argued on rehearing that the IMO and Ontario were in fact affiliated entities. September 2002 Order, 100 FERC ¶61,345 at ¶12, JA 1765. If affiliated,

Ontario could only obtain market-based rate authority by showing that the IMO adequately mitigated its market power through a tariff offering open access transmission with comparable service to all users. Initial Order, 99 FERC at 61,146, JA 88. In this context, Ontario would have to show that the IMO offers non-discriminatory access to its transmission system that can be used by competitors of Ontario to reach United States loads. September 2002 Order, 100 FERC ¶¶61,345 at ¶13, JA 1765-66.

The Commission ordered supplemental briefing on the issue of affiliation between Ontario and the IMO. *Ontario Energy Trading International Corp.*, 100 FERC ¶¶61,016 (2002). In its supplemental brief, Consumers argued again that the IMO was not independent of Ontario, but that they were affiliates. *See* R. 21 at 4-9, JA 108-12. Consumers further argued that the IMO did not provide service comparable to Order No. 888 standards because the IMO does not permit reservation of firm transmission capacity. *Id.* at 9-14, JA 112-17.

In the September 2002 Order, the Commission *agreed* with Consumers that the IMO and Ontario were affiliated, and therefore required Ontario to demonstrate that the IMO provides open access transmission service on a comparable, non-discriminatory basis. 100 FERC ¶¶61,345 at ¶12, JA 1765 (“Because Ontario owns all of the shares of Ontario Energy’s parent company, OPG, all of the shares of Hydro One, and is responsible for appointing the IMO’s Board, we find that Ontario Energy is an affiliated entity.”).

The Commission, however, rejected Consumers’ argument that the IMO service was not comparable to the standards established in Order No. 888. September 2002

Order, 100 FERC ¶¶61,345 at ¶13, JA 1765. A Canadian affiliate of a power marketer is not required to operate under an Order No. 888 tariff; rather, it is only required to offer non-discriminatory access to its transmission system that can be used by competitors of the power marketer to reach the United States. *Id.* (citing *H.Q. Energy Services (U.S.), Inc.*, 79 FERC ¶¶61,152 (1997); *Energy Alliance Partnership*, 73 FERC ¶¶ 61,019 (1995)). Under that standard, the Commission found that the IMO does provide open access transmission service on a comparable, non-discriminatory basis for any user seeking to wheel through and out of the Province of Ontario, sufficient to mitigate the IMO's transmission market power. *Id.*

Having prevailed on the issue of affiliation, Consumers did not raise the issue of the IMO's alleged lack of independence in its request for rehearing of the September 2002 Order. *See* R. 26, JA 1767-79. Consumers conceded that non-discriminatory access is guaranteed under Ontario's Electricity Act, and the IMO "may very well provide the same service to every utility on a non-discriminatory basis." *Id.* at 5-6, JA 1771-72.

Nonetheless, Consumers continued to argue that the IMO's service was not comparable to transmission service provided in the United States because the IMO does not allow reservation of firm transmission capacity while Ontario may reserve firm transmission capacity with its United States transmission providers. Consumers contends the inability to reserve firm transmission capacity causes it to face potential price uncertainty as a competitor in the Michigan market, at least for that portion of its energy supplies that it transports through the IMO/New York interconnection. *Id.* at 6-8, JA 1772-74. According to Consumers, a generation capacity shortage on the Michigan side

of the interconnect and a surplus on the New York side may produce locational price differences in the IMO market, *i.e.* price increases by way of congestion charges at the Michigan intertie, which could deprive Consumers of the economic gain it might otherwise capture for selling lower cost New York supplies in the Michigan market. *Id.* at 8, JA 1774. Consumers also argued that the IMO's bid-based system is not really comparable to that of the New York ISO because another affiliate of the IMO, with a large share of generation capacity, might manipulate prices. *Id.* at 9, JA 1775.

On rehearing, the Commission found that Ontario's Electricity Act guarantees open access to the IMO's system, and that Consumers had produced no evidence to suggest that the IMO is operating its system on a discriminatory basis. *See* April 2003 Order, 103 FERC ¶ 61,044 at ¶ 9, JA 1785 (citing The Electricity Act of 1998, at §§ 1(b) and 5(1)). The Commission rejected Consumers' lack of comparability claims as insufficient to support a finding that the IMO's transmission system design *per se* unduly impedes Consumers, or any other Ontario competitor, from reaching United States loads. *Id.* at ¶ 10. To the contrary, evidence showed at least 12 United States-based wholesale marketing companies trade successfully in and out of the IMO-administered markets by the way of the Michigan-Ontario interties. *Id.*

Further, although the IMO does not offer Order No. 888 point-to-point service, the Commission found that the IMO through its market rules does permit customers to obtain comparable service, *i.e.* firm point-to-point service through and out of Ontario at a price that is known in advance. *Id.* at ¶¶ 11-13, JA 1785. Thus, the Commission was satisfied that the Ontario IMO provides open access transmission on a comparable, non-

discriminatory basis for wheeling through and out of the Province of Ontario. Accordingly, Ontario's affiliation with the IMO does not provide a basis to deny Ontario's application for market-based rates. *Id.* at ¶ 13, JA 1785.

SUMMARY OF ARGUMENT

The Commission approves applications for market-based rates if the seller and its affiliates do not have, or adequately have mitigated, market power in generation and transmission, and cannot erect other barriers to entry by potential competitors. To demonstrate the absence or mitigation of transmission market power, a seller must show that a transmission-owning affiliate has an open access transmission tariff for the provision of comparable services.

Consumers does not deny that Ontario's transmission-owning affiliate, the IMO, is statutorily required to operate its transmission system on an open access, non-discriminatory basis. Indeed Consumers concedes that the IMO "may very well" provide non-discriminatory service.

Nevertheless, Consumers contends that the IMO's service available to Consumers is not comparable to that available to Ontario in the United States because the IMO's service does not duplicate the firm point-to-point service available under an Order No. 888 *pro forma* tariff. However, recognizing that it cannot dictate to Canadian entities how transmission services in Canada should be provided, the Commission has declined to require Canadian utilities to implement Order No. 888 *pro forma* tariffs, taking instead a flexible approach to the issue of whether Canadian entities offer comparable service.

Here, the Commission determined that the IMO's market rules permit customers, like Consumers, to obtain firm point-to-point service through and out of Ontario at a price that is known in advance, through placement of minimum (import) and maximum (export) bids and advance purchase of FTRs. The Commission reasonably concluded that this firm

point-to-point service, at a price known in advance, was comparable to the firm point-to-point transmission service provided under the Order No. 888 *pro forma* tariff. The Commission also found that the IMO's use of a bid-based structure with FTR hedging rights is comparable to the rights utilized by the New York and PJM ISOs, which the Commission had previously accepted as consistent with or superior to the provisions of the Order No. 888 *pro forma* tariff.

Consumers also argues that Ontario's affiliate OPG has such a large generation market share that it can cause constraints and congestion-related price differentials at export connections, and thereby erect barriers to Consumers' ability to compete with Ontario in wheeling power through the Ontario Province. The Commission found no evidence that Consumers has or will be so impeded. To the contrary, at least 12 United States-based wholesale marketing companies were already trading successfully in and out of the IMO-administered markets by way of the interties that Consumers would use. The Commission judged the contention that OPG would use its generation share to create barriers to Consumers' entry in the market "speculative" and lacking in even indirect or circumstantial evidence linking OPG's market share to increased prices or discriminatory treatment.

In an effort to buttress its lack of comparability argument, Consumers contends for the first time in its brief that the IMO cannot provide service comparable to United States RTOs because the IMO fails to meet the independence requirements for RTOs set forth in Order No. 2000. However, as Consumers failed to raise this argument before the Commission, the Court lacks jurisdiction to hear it. In any event, the argument lacks

merit because Ontario is not required to demonstrate that the IMO would meet United States RTO standards in order to show mitigation of the IMO's transmission market power. The Commission has never sought to apply its RTO standards to Canadian entities, rather, as with any affiliate, the IMO's tariff and service are judged to determine mitigation of the IMO's market power. Here, as discussed above, the Commission reasonably concluded that the IMO's market power is adequately mitigated because the IMO's governing statute and tariff provide for open, non-discriminatory access and comparable service.

Consumers points to Commission decisions, issued prior to restructuring of the Ontario power markets, rejecting Ontario Hydro's efforts to obtain service under United States utilities' open access tariffs because Ontario Hydro did not provide reciprocal open access service. Consumers asserts that nothing substantive has changed in the Ontario electricity market since that time because the Province of Ontario still owns the restructured Ontario utilities, and therefore Ontario must still be regarded as not providing reciprocal, comparable service. This overlooks the legislative restructuring of the Ontario electricity markets, which led to an IMO tariff guaranteeing reciprocal open access service. Thus, the issue in the prior Commission orders -- the lack of reciprocal service in Ontario -- no longer exists. Rather, the IMO is compelled by statute and tariff to provide open, non-discriminatory access to transmission, and the IMO's service meets the Commission's comparability standards for reciprocal service.

ARGUMENT

I. STANDARD OF REVIEW

The Court's review of the Commission's award of market-based rate authority is "limited to determining whether FERC's decision was 'arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.'" *Louisiana Energy and Power Authority v. FERC*, 141 F.3d 364, 366 (D.C. Cir. 1998). The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. Federal Power Act § 313(b), 16 U.S.C. § 825l(b).

II. THE COMMISSION PROPERLY GRANTED MARKET-BASED RATE AUTHORITY TO ONTARIO.

A. The Commission Reasonably Found That The IMO's Governing Statute And Tariff Require Open And Non-Discriminatory Access, And The IMO's Service Met The Comparability Requirement.

In a competitive market, the Commission may rely on market-based rates, in lieu of cost-of-service regulation, to provide rates that are just and reasonable. *Louisiana Energy*, 141 F.3d at 365. The Commission approves applications for market-based rates only if the seller and its affiliates do not have, or adequately have mitigated, market power in the generation and transmission of energy, and cannot erect other barriers to entry by potential competitors. *Id.* "To demonstrate the requisite absence or mitigation of transmission market power, the Commission normally requires a power marketer to show that a transmission-owning utility affiliate has on file with the Commission an open access transmission tariff for the provision of comparable services." *TransAlta Enterprises*,

Corp., 75 FERC ¶ 61,268 at 61,875 (1996). *See also AEP Power Marketing, Inc.*, 97 FERC ¶ 61,219 at 61,969 (2001).

Consumers does not deny that the IMO is statutorily required to operate its transmission system on an open access, non-discriminatory basis. April 2003 Order, 103 FERC at 61,174 and n.9, JA 1785 (citing The Electricity Act, 1998 at §§1(b) and 5(l)). Consumers indeed concedes that “the IMO may very well provide the same service to all utilities on a non-discriminatory basis, regardless of whether such utility is domestic or foreign.” Br. at 20.

Nevertheless, Consumers contends that the IMO does not provide comparable service because its service does not replicate firm Order No. 888 point-to-point service, like that offered by the Midwest ISO. *See* Br. at 22-23. According to Consumers, “Buy/Sell transactions offered by the IMO simply are not comparable with the reservation of transmission service that would otherwise be available to Ontario Energy in the United States.” Br. at 24. Consumers also argues that Ontario’s affiliated company holding generation assets, OPG, has such a large generation market share that it can cause “constraints and congestion-related price differentials at various export connections,” and, therefore, erect barriers to Consumers’ ability to compete with Ontario in wheeling power through the Ontario Province. *Id.* Neither argument has merit.

1. The Commission Reasonably Found IMO Service Comparable.

The Commission reasonably rejected Consumers’ contention, *see* Br. at 22-24, that the buy/sell transactions offered by the IMO were not comparable to the reservation

of transmission service available to Ontario in the United States under an Order No. 888 *pro forma* tariff. See April 2003 Order, 103 FERC ¶ 61,044 at ¶¶ 11-13, JA 1785.

First, the Commission has declined to require Canadian utilities to implement Order No. 888 *pro forma* tariffs, so long as they satisfy FERC's reciprocity requirements for comparable service. September 2002 Order, 100 FERC ¶ 61,345 at ¶ 13, JA 1765. Recognizing that it cannot dictate to Canadian entities how transmission services in Canada should be provided, the Commission has taken a flexible approach to the issue of whether Canadian entities offer comparable service. See Order No. 888-A at 30,292; *TransAlta*, 75 FERC at 61,875; *Energy Alliance*, 73 FERC at 61,030-31; *Ontario Hydro Interconnected Markets, Inc.*, 78 FERC ¶ 61,369 at 62,528 (1997). As Consumers itself recognized, "the Commission has stated that it will not require Canadian transmission owners to file Order No. 888 tariffs but, instead, is 'amendable to a variety of approaches,' and will review Canadian open-access regimes on a case-by-case basis to determine whether open-access transmission is being provided. . . ." Supplemental Protest of Consumers Energy Company, R. 9 at 4, JA 69 (citing *TransAlta*, 75 FERC at 61,875).

Here, the Commission reasonably concluded that the IMO's market rules permit all users to obtain firm point-to-point service through and out of Ontario, at a price that is known in advance, comparable to the firm transmission service provided under an Order No. 888 *pro forma* tariff, albeit through a different process. April 2003 Order, 103 FERC ¶ 61,044 at ¶ 13, JA 1785.

In the IMO's bid-based market, requests for transmission service are an integrated part of market participants' energy bids, thereby eliminating the need for a separate

transmission reservation mechanism, such as that utilized under the Order No. 888 *pro forma* tariff. See April 2003 Order, 103 FERC ¶ 61,044 at ¶ 11, JA 1785; Brief of Ontario Energy Trading International Corp., R. 20 at 8-11, JA 129-32. To obtain point-to-point transmission service, a market participant simultaneously bids to buy and sell into the export and import markets. April 2003 Order, 103 FERC ¶ 61,044 at ¶ 13, JA 1785.⁵ This point-to-point service can be made firm by submitting a minimum price bid to sell power into the import market and a maximum price bid to purchase the power for export. R. 20 at 16, JA 137; April 2003 Order, 103 FERC ¶ 61,044 at ¶ 13, JA 1785.

The IMO market rules further allow the market participant to obtain a firm price in advance for this point-to-point transaction. April 2003 Order, 103 FERC at 61,174 n. 11, JA 1785. In the absence of intertie congestion, the market participant would both sell power at the import intertie and buy power at the export intertie at the uniform system-wide Ontario price, which would net out, leaving the only charge for the transmission the export fee,⁶ April 2003 Order, 103 FERC ¶ 61,044 at ¶ 11, JA 1785; R. 20 at 8, JA 129, which the participant would know in advance of the transaction. April 2003 Order, 103 FERC at 61,174 n. 11, JA 1785.

⁵ For example, to transit energy from New York to Michigan through Ontario, a participant would simultaneously bid to sell (import) into Ontario at the New York intertie and purchase (export) from Ontario at the Michigan intertie. R. 20 at 16, JA 137.

⁶ The export fee is composed of three elements: (a) a pro-rata share of the IMO administrative costs; (b) a pro-rata share of other operating costs, such as internal Ontario congestion management; and (c) a charge of CDN\$1/MWh which covers a portion of the fixed cost of the transmission system. R. 20 at 16, JA 137.

If there is congestion at an intertie, the IMO sets an IZP calculated so that supply and demand clear the market. April 2003 Order, 103 FERC ¶ 61,044 at ¶ 12, JA 1785; R. 20 at 8, JA 129. If the congestion occurs at an export intertie, the IZP would exceed the internal Ontario price, and the cost for transmission of the through and out transaction would be the export fee and the difference between the IZP price and the uniform Ontario price. April 2003 Order, 103 FERC ¶ 61,044 at ¶ 12, JA 1785; R. 20 at 16, JA 137. Although congestion at interties therefore creates a risk of price volatility, the IMO auctions FTRs that allow participants to hedge this risk. April 2003 Order, 103 FERC ¶ 61,044 at ¶ 12, JA 1785. An FTR holder receives payments for a congestion-related price differential at a specific intertie zone equal to the difference between the uniform system-wide internal Ontario price and the IZP price. *Id.*

Thus, FTRs offset congestion costs incurred by the holder (dollar for dollar) with revenues from the FTR, so that the revenues that the customer receives for its imports will exactly offset the costs that it must pay for its exports. *Id.* at n. 11. The net cost to the customer is the export fee plus the cost of acquiring FTRs, both of which the customer would know prior to its through and out transaction. *Id.*

Consequently, the Commission reasonably concluded that the IMO's market rules permit customers to obtain comparable firm point-to-point service through and out of Ontario at a price that is known in advance, through placement of minimum (import) and maximum (export) bids and advance purchase of FTRs. *Id.* at ¶ 13. *See Remediating Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design*, 100 FERC ¶61,138 at ¶144 (2002) ("SMD Order") (network

access service, coupled with congestion revenue rights to offset congestion charges, provides the customer with certainty with respect to delivery and price). Because any market participant, including Consumers, is therefore able to obtain firm transmission service in the IMO market, this refutes Consumer's contention that its inability to reserve transmission capacity on the IMO system to transit energy from New York to Michigan creates a "barrier" that "effectively" removes Consumers as a competitor in the Michigan market. Br. at 21-22.

The Commission also found that the IMO's use of the bid-based structure with FTR hedging rights is comparable to the rights utilized by the New York and PJM ISOs, which the Commission had previously accepted as consistent with or superior to the provisions of the Order No. 888 *pro forma* tariff. April 2003 Order, 103 FERC ¶ 61,044 at ¶ 12, JA 1785. ⁷ Indeed, the Commission has recognized that "[t]he *pro forma* tariff was envisioned as the baseline above which transmission providers were encouraged to develop competitive and customer-responsive service offerings," and that, *inter alia*, PJM and the New York ISO had produced more beneficial market development than the

⁷ Both the New York ISO and PJM utilize a locational-based marginal pricing system, under which separate energy prices are determined at each node equaling the marginal cost to the ISO of producing and delivering energy to the node, based on bids submitted in an energy auction. See *Central Hudson & Gas Electric Corp.*, 86 FERC ¶ 61,061 at 61,222-23 (1999). The IMO market rules utilize functionally the same approach, with the internal Ontario market effectively constituting one node, and the interties constituting separate nodes. Also similar to the IMO, rather than adopt the firm reserved transmission service contemplated under the Order No. 888 tariff, the New York ISO and PJM adopted financial instruments that allow participants to hedge against congestion costs. *Id.* at 61,206.

Midwest ISO, SMD Order, 100 FERC ¶¶61,138 at ¶¶ 34-35, upon which Consumers relies as the benchmark for what open access service must be offered. Br. at 22.

2. OPG’s Generation Market Share in Ontario Does Not Alter the Comparability Analysis.

Consumers contends that the IMO cannot provide comparable service because, unlike the New York ISO which has multiple generation sources, the IMO has an affiliate, OPG, with the generation market power to “manipulate pricing,” Br. at 16, and to cause “constraints and congestion-related price differentials at various export connections,” and thereby to erect barriers to prevent Consumers from effectively competing with Ontario, Br. at 24-25. Consumers asserts that the IMO buy/sell model would, particularly in the event of generation capacity shortage in Ontario, result in higher prices for power exported to Michigan, thereby undercutting Consumer’s ability to reap the advantage of transporting cheaper New York power to Michigan. Br. at 23. The Commission reasonably rejected these arguments. April 2003 Order, 103 FERC ¶¶61,044 at ¶ 10 and n. 10, JA 1785.

In order to obtain market-based rate authority, Ontario must demonstrate that the IMO offers non-discriminatory wholesale access to its transmission system that can be used by competitors of the power marketer to reach the United States. September 2002 Order, 100 FERC ¶ 61,345 at ¶ 13, JA 1765 (citing *Energy Alliance Partnership*, 73 FERC at 61,030-31).⁸ The Commission found “no evidence in this case that Consumers

⁸ As explained in *Energy Alliance*, the Commission is not concerned with service of Canadian loads, which are beyond its jurisdiction, but rather only with transmission service for United States loads. *Energy Alliance*, 73 FERC at 61,030. Thus, the

has or will be impeded from reaching the Michigan markets.” April 2003 Order, 103 FERC ¶61,044 at ¶10, JA 1785. To the contrary, “there have been at least 12 U.S.-based wholesale marketing companies trading successfully in and out of the IMO-administered markets, to date (since the IMO began operating on May 1, 2002), by way of the Michigan-Ontario interties.” *Id.*

The Commission found that Consumers’ allegation that OPG would use its generation share to create barriers to Consumers’ entry in the market to be “speculative” and lacking in even indirect or circumstantial evidence that linked OPG’s market share to increased prices or discriminatory treatment. April 2003 Order, 103 FERC at 61,174 n. 10, JA 1785.

Indeed, the IMO’s market rules eliminate OPG’s ability or incentive to utilize its generation market power to create transmission congestion in an effort to drive up prices to Consumers’ detriment. First, OPG has no ability to exercise its generation market power within Ontario in a manner that will create barriers to Consumers because, in a through and out transaction, Consumers would sell power at import and buy it back at export at the same uniform Ontario market price, netting out to zero. April 2003 Order, 103 FERC at 61,174 n. 11, JA 1785. Thus, even if a generation shortage in Ontario produced higher prices for generation, *see* Br. at 23, the higher price Consumers would pay for export power would be cancelled out by the higher price Consumers would

Commission is concerned with the service competitors of the power marketer receive in transmitting power from Canada into the United States. *Id.*

receive for import power. Internal congestion does not create a congestion-driven price differential because the IMO sets the internal, system-wide price based on the marginal cost of generation in an unconstrained dispatch solution, and spreads the cost of congestion among all users through a uniform uplift charge. R. 20 at 11-12, JA 132-33.

Under the IMO market rules OPG similarly lacks incentive or ability to impede Consumers' transactions by using its Ontario generation market power to drive up congestion costs at the interties. OPG has no generation market power outside of Ontario (hence the finding that Ontario's market-based rate application presents no issues of generation market power).⁹ Initial Order, 99 FERC at 61,146, JA 88. In order to export power, OPG, like all other market participants, has to sell its generation into the IMO pool at the uniform Ontario price, at the location of its generation resource, and then buy power for export at an intertie. *See* R. 1, Exhibit, Affidavit of Cliff W. Hamal, at 9 ¶ 18, JA 43; R. 20 at 15, JA 136. If OPG creates congestion at the intertie, OPG would receive the uniform Ontario price for its generation, but would have to pay the higher IZP price at the intertie, leaving a net payment to the IMO equal to the difference between the two prices. R. 20 at 15, JA 136. *See* April 2003 Order, 103 FERC ¶ 61,044 at ¶ 12, JA 1785. Thus, while OPG theoretically could submit bids in sufficient quantities to congest an intertie out of Ontario, that would increase OPG's own congestion costs to export its power, and then OPG would have to market in the United States (where it has no market power)

⁹ At this time OPG sold approximately 99 percent of its generation in the Ontario market. R. 13, Answer of Ontario Energy Trading International Corp. in Opposition To Late-filed Motion to Intervene, at 10, JA 1760.

power made more expensive as a result of those congestion charges. Thus, it would receive no advantage over Consumers in this unlikely and speculative scenario.

Further, Consumers, like any other market participant, can protect itself from congestion cost increases by buying FTRs. April 2003 Order, 103 FERC ¶ 61,044 at ¶ 12, JA 1785. Any effort by OPG to increase congestion costs would not affect FTR holders. R. 20 at 20, JA 141. OPG has no market power with regard to FTRs because they are sold at auction. *Id.*¹⁰

Thus, in light of the IMO's market rules and market structure, OPG lacks ability or incentive to attempt to benefit Ontario by creating barriers to Consumers' competing through and out transactions. Conversely, Consumers' claims of manipulation are "not accompanied by *any* evidence (direct or even circumstantial) tying OPG's alleged market shares to either increased transmission prices or discriminatory conduct of any kind on the part of the IMO." April 2003 Order, 103 FERC at 61,174 n. 10, JA 1785. Thus, the Commission correctly concluded that it is highly speculative whether such manipulation would occur, and even if it did, whether it would impede Consumers' ability to compete with Ontario through wheeling power through the Ontario Province.

¹⁰ Further, even if OPG theoretically could attempt to raise the cost of transmission rights by submitting large bids for those rights, that would likewise result only in increasing OPG's own costs which would make its own power less competitive in the United States markets. *Id.*

B. Consumers' Argument That The IMO's Lack Of Independence Renders Its Service Not Comparable To United States RTOs Was Not Raised To FERC, And, In Any Event, Lacks Merit.

In an effort to buttress its lack of comparability arguments, Consumers contends for the first time in its brief that the IMO cannot provide service comparable to United States RTOs or ISOs because the IMO fails to meet the independence requirements for RTOs set forth in Order No. 2000.¹¹ *See* Br. at 17. This argument fails on a number of levels.

First, the Court lacks jurisdiction to hear this argument. Before the Commission, Consumers argued only that the IMO's lack of independence required a finding that the IMO and Ontario were affiliated, *see* R.19 at 4-9, JA 108-12, a point on which Consumers *prevailed* in the September 2002 Order. 100 FERC ¶ 61,345 at ¶ 12, JA 1765 ("Because Ontario owns all of the shares of Ontario Energy's parent company, OPG, all of the share of Hydro One, and is responsible for appointing the IMO's Board, we find that Ontario Energy is an affiliated entity."). Having *prevailed* on this point, Consumers did not raise this new argument -- that the IMO's alleged lack of independence rendered it unable to provide comparable service -- in its request for rehearing of the September 2002 Order, in which the Commission found that the IMO provided comparable, non-discriminatory service. *See* R. 26, JA 1767-79.

Consequently, the Commission never had occasion to address the claim that the IMO's lack of independence -- besides showing the IMO and Ontario are affiliated -- also

¹¹ *Regional Transmission Organizations*, Order No. 2000, FERC Stats. & Regs. ¶31,089 (1999), *on reh'g*, Order No. 2000-A, FERC Stats. & Regs. ¶31,092 (2000).

would preclude a finding that the IMO's service was comparable. *See* April 2003 Order, 103 FERC ¶ 61,044, JA 1783-85. As this issue was not raised on rehearing, the Court lacks jurisdiction to consider it. Federal Power Act § 313(b), 16 U.S.C. § 8251(b) ("[n]o objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure to do so"). *See also City of Orrville, Ohio v. FERC*, 147 F.3d 979, 990 (D.C. Cir. 1998) (court lacks jurisdiction to hear arguments not made on rehearing); *Platte River Whooping Crane Critical Habitat Trust v. FERC*, 876 F.2d 109, 113 (D.C. Cir. 1989) (parties seeking review must themselves raise on rehearing all objections urged on appeal).

Second, Consumers' argument is without merit. Contrary to Consumers' protestations, *see* Br. at 14-17, the Commission never found that the IMO met the Order No. 2000 independence standards.¹² Indeed, if the Commission had ultimately found the IMO independent, as it did in the Initial Order, no further inquiry would have been required as to Ontario's transmission market power. *See* Initial Order, 99 FERC at 61,146-47, JA 88-89. Rather, the fact that the Commission could not find the IMO independent required inquiry into whether the IMO's transmission market power was adequately mitigated. September 2002 Order, 100 FERC ¶ 61,345 at ¶ 12, JA 1765.

¹² Consumers finds this purported "holding" in a footnote stating that the IMO is a "not-for-profit transmission and market operator whose duties and functions, beginning on May 1, 2002, would be similar to those of a regional transmission organization in the United States." April 2003 Order, 103 FERC at 61,172 n.3, JA 1783. *See* Br. at 14 and n. 42.

To show mitigation of the IMO's transmission market power, Ontario is not required to demonstrate that the IMO would meet the same standards governing United States RTOs. The Commission has never sought to apply its RTO standards to Canadian entities, recognizing Canada's sovereign authority over Canadian entities and transactions taking place in Canada. *See, e.g.*, Order 2000 at 31,203.¹³ Rather, as with any affiliate, the IMO's tariff and service is judged to determine whether the IMO's market power is adequately mitigated. September 2002 Order, 100 FERC ¶ 61,345 at ¶¶12-13, JA 1765. Recognizing that it should not dictate to Canadian entities how transmission services should be provided, the Commission has taken a flexible approach to the issue of whether foreign entities have adequately mitigated their market power. *See* Order No. 888-A at 30,292; *TransAlta*, 75 FERC at 61,875; *Energy Alliance*, 73 FERC at 61,030-31; *Ontario Hydro Interconnected Markets, Inc.*, 78 FERC at 62,528. Here, as discussed above, the Commission reasonably concluded that the IMO's market power is adequately mitigated

¹³ Although the Canadian IMO is not subject to U.S. RTO standards, the composition of the IMO's Board is not comparable to that of the California ISO Board rejected in *Mirant Delta LLC*, 100 FERC ¶61,059 (2002). *See* Br. at 15-16. In California, all five Board members were selected by the Governor and served at his pleasure, and three of the five were current or former state officials where the State was the largest purchaser of electricity in California. *Mirant Delta*, 100 FERC at ¶10. Accordingly, the California ISO Board's decision-making was "heavily influenced, if not completely dictated, by one stakeholder (*i.e.* the State)." *Id.* at ¶50.

In contrast, while the Ontario Minister of Energy, Science and Technology appoints the IMO's Board, members can be removed only for cause. *See* Electricity Act, §§7(2)(b); 7(6); R. 1 at 7, JA 13. No employees of the Government were appointed, and eight of the seventeen Board members are independent of any market participant. R. 1 at 8, JA 14. Of the remaining nine members representing stakeholders, OPG only has one seat. *Id.* at 12. A stakeholder board does not affect RTO independence so long as no party or market segment has undue representation. *See* Order 2000 at 31,073-74.

because the IMO's governing statute and tariff provide for open, non-discriminatory access and comparable service.

Consumers points to Order No. 888-A and *Promoting Wholesale Competition*, 79 FERC ¶61,367, in which the Commission rejected Ontario Hydro's efforts to obtain service under United States utilities' open access tariffs without providing reciprocal open access service. Br. at 17-18. Consumers asserts that "[n]othing substantive has changed in the Ontario electricity market" since that time because the Province of Ontario still owns the restructured Ontario utilities, and therefore Ontario must still be regarded as not providing reciprocal, comparable service. Br. at 18. This overlooks the legislative restructuring of electricity markets, which led to an IMO tariff that guarantees reciprocal open access service. Thus, the fundamental issue in Order No. 888-A and *Promoting Wholesale Competition* -- the lack of reciprocal service in Ontario -- no longer exists. Consumers therefore errs in stating that "U.S. entities like CECo can only obtain entrance into and through Ontario markets on transmission access terms and conditions dictated by Ontario Energy's government controlled transmission affiliate." Br. at 17. Rather, the IMO is compelled by statute and tariff to provide open, non-discriminatory access to transmission, and the IMO's service meets the Commission's comparability standards for reciprocal service.

CONCLUSION

For the reasons stated, the Commission's orders should be affirmed in all respects.

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CERTIFICATE OF COMPLIANCE

In accordance with Circuit Rule 28(d)(1), I hereby certify that this brief contains 7551 words, not including the tables of contents and authorities, the certificate of counsel, this certificate and the addendum.

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