Florida Power & Light Company, Docket Nos. ER93-465-006, ER93-922-004, ER93-507-003, EL93-28-002, EL93-40-002, and EL94-12-002

[61,477]

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Florida Power & Light Company, Docket Nos. ER93-465-006, ER93-922-004, ER93-507-003, EL93-28-002, EL93-40-002, and EL94-12-002

Order on Rehearing

(Issued February 10, 1995)

Before Commissioners: Elizabeth Anne Moler, Chair; Vicky A. Bailey, James J. Hoecker, William L. Massey, and Donald F. Santa, Jr.

[61,478]

I. Introduction

This case originated with a comprehensive rate filing (in Docket No. ER93-465-000) by Florida Power & Light Company (FPL) that was intended to restructure existing rates for various types of wholesale power and transmission service. The rate filings included unilateral revisions to FPL's existing wholesale electric service tariff, FPL's interchange contracts, certain specific transmission service agreements and related rate schedules with various wholesale customers. FPL also filed new tariffs available to all other utilities and generators for bulk power wholesale transmission services.

Later, in Docket No. ER93-922-000, FPL filed revised rates incorporating formula rates for seven long-term transmission agreements with various customers.

The Commission has issued several orders in proceedings that originated with these two filings; those orders will be addressed where appropriate below.

This order addresses requests for rehearing and requests for clarification arising out of three orders issued in this multi-faceted proceeding, on February 24, 1994, June 16, 1994, and August 4, 1994, respectively. [1]

For the reasons set forth below, we will: (1) grant rehearing of the February 24 Order to the extent that we are modifying the length of time FPL must use to calculate opportunity costs; (2) deny rehearing concerning FPL's proposed restriction on the resale of power by its partial requirements customers; and (3) set for hearing the question of whether the divisor for calculation of non-customer specific rates should be something other than the annual system peak. We also will clarify as necessary certain aspects of earlier orders.

In addition, we will deny the rehearings of the June 16 Order and the August 4 Order.

II. Background

A. *The September 24 Order*

On September 24, 1993, the Commission accepted FPL's proposed rates in Docket No. ER93-465-000 (as modified) for filing, suspended them for five months to become effective February 26, 1994, subject to refund, and set them for hearing. [2] The issues set for hearing included whether "FPL's filing will have anticompetitive effects on the wholesale bulk power markets in peninsular Florida." [3] The Commission also set for hearing all other issues (except one) raised in FPL's filing and the responsive pleadings. The one issue that was not set for hearing (in addition to the generic transmission pricing issues discussed below) was whether FPL's proposed rates were unjust and unreasonable because the proposed tariff does not provide for network service. That issue was addressed on rehearing in the Commission order of June 16, 1994, discussed below. [4]

B. *The February 24, 1994 Policy Order*

Due to the complexity and magnitude of FPL's filing, [5] the Commission also stated in the September 24, 1993 order that it had decided to issue a supplemental order on seven generic pricing issues that did not require a trial-type evidentiary hearing. On February 24, 1994, the Commission issued that supplemental order. [6] In the Policy Order, the Commission: (1) allowed FPL to keep in its tariff a resale price cap at the price (and not higher) at which FPL first sold the transmission service to the transmission customer (which is now reselling to its own customer); (2) ordered FPL to calculate opportunity costs on a life-of-the-transaction basis, rather than an hourly basis; (3) allowed FPL to set rates for short-term (one year or less) firm transmission services at the higher of its embedded or opportunity costs without an expansion cost cap; (4) ordered FPL to remove the tariff provision (because it is overly broad) that restricts sales by partial requirements

[61,479]

(PR) customers to the economy energy market, when FPL's incremental production costs exceed its incremental revenues; (5) ordered FPL to revise its formula to use its annual system peak (not the average of its 12 monthly system peaks) as the divisor in its transmission rate formula; (6) ordered FPL to revise its formula to reflect the Commission's requirement that the production component of hourly rates be developed by dividing annual fixed costs by 8,760 hours per year; and (7) ordered FPL to revise its formula rate so that demand and energy charges reflect the cost of the same generating resources--i.e., to reflect the fixed costs of the generating units that are reflected in the incremental cost energy charge, weighted on relative use.

Pending Rehearings of the Policy Order

On March 28, 1994, requests for rehearing of the Policy Order were filed by the following parties: FPL, Seminole Electric Cooperative, Inc. (Seminole), Florida Cities, [7] and the Florida Public Service Commission (Florida Commission). The requests pertain to Issues 2, 4, and 5 enumerated above. The parties' position on each issue on rehearing will be explained in detail in the following Discussion section, immediately preceding the resolution of each issue.

C. *The June 16, 1994 Order*

Several parties (FPL, Florida Cities, Florida Commission, the City of New Smyrna Beach, Florida (New Smyrna), and Seminole) filed requests for rehearing of the September 24 Order. The arguments are discussed in detail in the June 16 Order. The main arguments concerned whether FPL should provide network service in the tariff, and whether, under the *Mobile-Sierra* doctrine, [8] FPL is permitted by existing contracts to file proposed rate changes that unilaterally change from stated to formula rates. Florida Cities argued that FPL must provide network transmission service, and that, although it did not object to the Commission's considering the network transmission service question more fully in another pending proceeding, [9] FPL still had the burden in this proceeding to justify its failure to propose network service in its tariffs.

On June 16, 1994, the Commission issued an order addressing the requests for rehearing of the September 24 Order. The Commission emphasized that its findings concerning whether a utility has or lacks market power is a fact-specific determination, and that FPL's modeling its proposed tariff on other open-access transmission tariffs does not guarantee the Commission's acceptance of FPL's proposed tariff. The Commission also set for hearing: (1) precisely what services should be included in FPL's tariff in order to ensure that the tariff services are comparable to those services FPL provides itself, pursuant to the "comparability standard" set forth in *American Electric Power Service Corporation*; [10] and (2) certain *Mobile-Sierra* issues (governing FPL's contractual ability to revise its rates charged certain wholesale customers by substituting formula rates for its existing stated rates). [11]

Pending Rehearings of the June 16 Order

On July 18, 1994, requests for rehearing of the June 16 Order were filed by FPL and Tampa Electric Company (Tampa). FPL seeks rehearing of the Commission's decision in the June 16 Order to set for hearing whether FPL is barred from unilaterally filing amendments to certain rate schedules and tariffs under which it provides various services to Seminole. [12] FPL argues that the relevant rate schedules and the wholesale tariff contain language that expressly gives FPL the unrestricted right to file unilateral rate changes under section 205 of the Federal Power Act (FPA). FPL also argues that, since the rate schedules and tariff at issue clearly authorize the filings FPL has made in this proceeding, the Commission's decision to set this matter for hearing will create uncertainty for numerous similar contracts on file with the Commission and for ongoing contractual negotiations regarding the appropriate language sellers should use in order to reserve the right to make unrestricted rate changes.

Tampa argues on rehearing that the Commission should expand the scope of the evidentiary hearing (ordered in the June 16 Order) to require the parties, including FPL, to propose specific modifications to FPL's filed tariff and rate schedules needed to satisfy the *AEP* comparability standard. Tampa also argues that

[61,480]

FPL's restructured tariff (which became effective on February 26, 1994, subject to refund) already has resulted in competitive harms and that refund protection will not adequately redress such harms. Noting that FPL's restructured filing (with continued point-to-point service) will remain in effect until the implementation of a final Commission order in this proceeding resolving the comparability issue, Tampa requests that the Commission grant interim relief by ordering FPL to, among other things, apply the same rates, terms and conditions of service contained in its filed transmission tariffs to itself in making future wholesale power sales.

D. *The August 4, 1994 Order*

On August 4, 1994, the Commission issued an order [13] on requests for rehearing filed by FPL and by Seminole of the Commission's order issued on October 29, 1993, in Docket No. ER93-922-000. [14] In the October 29, 1993 order, the Commission accepted for filing, suspended, and set for hearing revised rates under transmission agreements between FPL and four of its transmission customers. The Commission also consolidated the proceeding in Docket No. ER93-922-000 with the ongoing proceeding in Docket No. ER93-465-000.

Citing its June 16 Order, the Commission found in the August 4 Order that the *Mobile-Sierra* issue raised on rehearing should be addressed at hearing, and that several other issues were moot because they had been resolved in the Policy Order and in the June 16 Order. The Commission emphasized that it has no inherent preference for stated rates over formula rates; *all* rates must meet the section 205 just and reasonable standard. [15]

Pending Rehearing of the August 4 Order

On September 6, 1994, FPL filed a request for rehearing of the August 4 Order. FPL explains that its rehearing is similar to that filed in its July 18, 1994 request for rehearing of the June 16 Order. [16] FPL repeats its request for rehearing of "the Commission's statement that it is 'unclear from the face of the contract' whether FPL has the contractual authority to seek certain waivers [i.e., to file formula rates instead of stated rates] that [Seminole] contends are necessary for the contract amendments FPL filed in this docket, and of the Commission's decision to set Seminole's *Mobile-Sierra* argument for hearing." [17] FPL also continues to dispute the Commission's finding that it is unclear from the contract whether FPL has the authority to file unilateral rate applications.

The only argument that differs from FPL's July 18, 1994 rehearing is its contention that, in the August 4 Order, the Commission erroneously stated that Seminole challenged FPL's right to file unilateral proposed rate changes. According to FPL, "[t]he only challenge to FPL's right to unilaterally change the rates . . . is Seminole's assertion that FPL cannot change from stated rates to formula rates." [18] FPL argues that, beyond that, no one has asserted that FPL does not have the right to file unilateral rate changes. FPL contends that the Commission's conclusion conflicts with section 35.1(d)(2) of the Commission's own regulations. [19] FPL also contends that Seminole is attempting to confuse the issues. FPL urges the Commission to clarify that FPL does have the authority to make the filings that it made.

E. *The Compliance Filing*

On April 11, 1994 (having been granted an extension of time), FPL made its compliance filing as directed by the Commission in the Policy Order. FPL amended the compliance filing on August 12, 1994. Protests were filed. We will address the issues directly concerning the compliance filing in a separate order to be issued in the near future. Accordingly, this order will not discuss the compliance filing.

III. Discussion

We will first address the rehearings of the Policy Order. Then we will address in turn the

[61,481]

rehearings of the June 16 Order and the August 4 Order, respectively.

A. *The Policy Order Rehearings*

Calculation of Opportunity Costs

Background

In the Policy Order, the Commission directed FPL to calculate opportunity costs on a life-of-the transaction basis, rather than on an hourly basis. The Commission maintained that, as explained in *New England Power Company, et al.,* [20] *hourly pricing "would allow a charge that is virtually as high as an 'and' price."* [21] *The Commission rejected FPL's argument that because firm transmission services are scheduled on an hourly basis and opportunity costs are incurred on an hourly basis, opportunity costs should be calculated on an hourly basis. The Commission stressed that "[t]he relevant fact is that while these services, as all services, are scheduled on an hourly basis, they are not contracted for, or evaluated on, an hourly basis."* [22] *The Commission also rejected FPL's contention that, because native-load customers pay both embedded costs and opportunity costs, transmission customers should do the same. The Commission cited to New England Power Company,* [23] *in which it found that an embedded cost transmission rate can include a pro rata share of all costs, including opportunity costs. Such a rate would be considerably lower than the rate proposed by FPL because all customers, both native load and transmission, would share the opportunity costs.* [24]

FPL requests rehearing on this issue, repeating its argument that the Policy Order ignores certain real time efficiencies that can only be evaluated on an hourly basis. FPL urges the Commission, on rehearing, to "explain why it disregarded short-term efficiencies and why its concerns as to the long-term impacts of FPL's proposal have any application to short-term transactions." [25]

FPL contends that life-of-the-transaction comparisons do not produce results that are consistent with cost causation. [26] FPL disagrees with the Commission's statement in the Policy Order that our pricing policy has been upheld by the DC Circuit in *Penelec.* FPL attempts to distinguish *Penelec*, claiming that "and" pricing was at issue in that case; but that the Commission has recognized that the hourly comparison of opportunity costs is a form of "or" pricing that does not result in a utility recovering twice for two uses of the same system. [27]

FPL also complains that the Policy Order fails to distinguish between FPL's Transmission Tariff No. 1 (for transactions with terms up to and exceeding 30 years) and FPL's Transmission Tariff No. 2 (for transactions with terms ranging from one day to one year). FPL argues that, at the very least, the Commission should not apply the life-of-the-transaction comparison to the short-term firm transactions under Tariff No. 2. According to FPL, because the life-of-the-transaction method is based on the utilities' evaluation of system expansion costs, it is not reasonable to apply it to short-term transactions: utilities do not use a system expansion cost analysis in deciding whether to enter into short-term transactions. FPL contends that, therefore, it should be able to use hourly comparisons for opportunity costs in the short-term transactions arising under Tariff No. 2.

Florida Cities request clarification or, in the alternative, rehearing of this issue. Florida Cities state that, while they generally accept the Commission's Policy Order, they request clarification concerning whether the Commission intended to allow a hearing on the issue of Florida Cities' possible liability for opportunity costs, or whether the Commission intended to deny summarily Florida Cities' request that this issue be set for hearing. If the Commission intended to deny Florida Cities' request for hearing, then Florida Cities request rehearing. Florida Cities contend that they should not pay opportunity costs in any case because, *inter alia*, they are transmission dependent customers, and FPL's St. Lucie License Conditions bar opportunity cost pricing. [28] Florida Cities stress that they have made numerous good faith yet unsuccessful attempts to invest directly in FPL's transmission system.

On April 12, 1994, Seminole filed an answer in support of Florida Cities' motion for clarification. Seminole and Florida Cities request clarification that the Policy Order did not "silently" resolve Florida Cities' arguments against opportunity cost pricing.

[61,482]

Resolution

The central issue raised by FPL on rehearing is the appropriate time period over which to compute the price for *firm* transmission service to third parties. According to FPL, the appropriate period for developing a firm transmission rate (i.e., for choosing between embedded costs or opportunity costs) is hourly--regardless of the term of the transaction. As discussed below, we disagree that an hourly comparison is appropriate. However, we will modify our prior approach.

FPL correctly notes that, in *Northeast Utilities Service Company*, the Commission permitted a non-firm price to be based upon hourly comparisons of embedded cost and opportunity cost. [29] But the Commission's decision in that case was based upon the fact that the transmitting utility had specifically reserved the right to curtail service to the non-firm transmission customer for any reason, including to take advantage of short-term economy transactions on behalf of its native load customers. Moreover, in such instances, the "embedded cost" rate that the non-firm transmission customer pays must be appropriately discounted [30] to reflect the fact that the transmission service is interruptible and inferior in terms of service priority to the transmission owner's uses of the system--including economy transactions the transmission owner undertakes on behalf of native load. [31] In the context of non-firm transmission service, opportunity cost pricing provides a mechanism for the non-firm transmission customer to avoid interruption by "buying through" and reimbursing the utility for any foregone revenues (or savings) associated with an economy transaction that cannot be simultaneously accommodated because the transmission system is constrained. In essence, the term of service to the non-firm transmission customer is hour-to-hour and the price is appropriately computed hour-to-hour.

In contrast, a firm transmission customer pays a firm transmission rate in order to use the transmission system in an uninterrupted manner for the term of the transaction. The Commission permits the utility, at its option, to develop a firm transmission rate based upon the higher of two potential measures of transmission cost responsibility. The utility may develop a transmission rate by either: (1) allocating a portion of the average, embedded cost transmission revenue requirement (including the cost of any necessary upgrades) to the third party transmission customer; or (2) specifically assigning any incremental costs that are incurred to provide the requested transmission service to the third party customer. In the context of firm transmission service, opportunity cost pricing is simply the measure of incremental cost responsibility when expansion of the system is not warranted.

FPL's reliance on cases where the Commission has permitted opportunity costs to be assessed on an hourly basis for *non-firm* transmission is misplaced. The transmission service at issue in this proceeding is *firm* service under which the transmission customer will purchase capacity rights to use FPL's system for the term of a contract. FPL should not be permitted to price firm transmission service as if it were non-firm hourly service.

By way of example, assume that a third-party transmission customer wants to purchase firm transmission for a period of one month under the proposed tariff. Under the Commission's existing interpretation of *NU* pricing, FPL may charge the customer an embedded cost rate for the month. Alternatively, if FPL can demonstrate that it incurs foregone opportunity costs during the month (which are solely attributable to the provision of service to the third-party transmission customer) that are higher than the revenues which it would collect under an embedded cost rate for the month, it may recover the foregone opportunity costs from the third-party transmission customer. But the Commission will not permit FPL to convert the one month request for firm service into 730 separate hourly "transactions" for pricing purposes.

Moreover, this is not the way that FPL prices transmission service to its native load customers and pricing that way for third-party transmission service would not be comparable. As the Commission stated in the Policy Order:

> While FPL is correct that native load pays opportunity costs as well as embedded costs, FPL's suggestion that native load pays the same rate that FPL proposes here is incorrect. No native-load customer pays both a pro rata share of embedded costs plus all of the opportunity costs that would not have been incurred but for that customer. Native load customers pay a pro rata share of all system-wide costs, both embedded costs and opportunity costs.[[32]]

[61,483]

FPL has made three specific allegations of error with regard to the Policy Order. First, FPL claims that the Commission ignored short-term efficiencies resulting from optimal dispatch and economy transactions. But the Commission did not ignore short-term efficiencies; it simply recognized that the dispatch efficiencies relevant in the context of commitments of firm transmission capacity to a third-party customer are the efficiencies over the entire commitment period. Second, FPL alleges that the Commission's life-of-transaction analysis fails to hold native load customers harmless. But, as the Commission has discussed at length in prior orders, under either scheme of revenue recovery (embedded costs or opportunity costs), native load customers are held harmless. Indeed, FPL's hourly comparison of embedded and opportunity costs could result in third party transmission customers subsidizing native load. Finally, FPL claims that the Commission did not provide a reasoned analysis as to why a life-of-transaction comparison should be applied to short-term (i.e., less than one year) firm transactions. But, as discussed above, FPL's proposal would transform any firm transmission request, regardless of the term of service requested, into hourly service for pricing purposes. We believe that forcing third-party transmission customers to pay for firm transmission service "by the hour"--regardless of the term of the transaction--is inappropriate.

While FPL has not demonstrated that an hourly comparison of embedded costs and opportunity costs is just and reasonable, upon further consideration, the Commission has concluded that forcing utilities to make such cost comparisons over the life of a long-term firm transmission contract is inappropriate. Accordingly, we will permit utilities proposing to charge the higher of embedded or opportunity costs for long-term firm transmission service (i.e., one year or more) to make the comparison based on a one-year period. For FPL, this will apply to service under Transmission Tariff No. 1, which provides for transactions with terms in excess of one year and up to thirty years. [33]

We have selected a twelve-month comparison on the basis of a number of factors. First, from the standpoint of administrative efficiency, a utility should be permitted to close its books of account after some reasonable period of time and not be subject to possible refunds or surcharges at the end of every long-term transmission contract. While it may be possible to avoid such a result through some form of automatic opportunity cost tracker clause, any such tracking mechanism raises a number of implementation, accounting, and monitoring issues. Allowing utilities to finalize accounting entries will provide certainty to both the utility (with regard to revenue recovery) [34] and to the transmission customer (with regard to cost exposure). Moreover, as the Commission noted in an earlier order discussing opportunity cost pricing:

> We simply cannot reasonably resolve challenges to opportunity costs long after such costs were incurred. For example, under a twenty-year contract, we cannot realistically review challenges in the tenth year for opportunity costs identified in the first year. Accordingly, we will require challenges to [the utility's] identification of opportunity costs to be raised within 90 days of the end of the calendar year. Absent such challenge, the opportunity costs identified in the prior calendar year will not be subject to challenge.[[35]]

Finally, the time period we have selected corresponds with the Commission's traditional method of establishing rates based upon twelve months of representative cost data for a "test period". [36]

The Commission wishes to stress, however, that our decision to allow FPL to charge the higher of embedded costs or opportunity costs calculated on an annual basis does *not* affect FPL's responsibility to develop and support an expansion cost estimate which will cap the total amount of revenues that FPL will be permitted to recover under any long-term firm transmission contract. The expansion cost estimate provides two important functions. First, it provides the transmission customer with a measure of the maximum transmission rate exposure it may face over the term of the contract. As the Commission noted in *American Electric Power Service Corporation*:

> [T]ransmission customers need rate certainty, and they need it for two reasons: (1) customers must have reliable information as to transmission costs in order to make economic decisions; and (2) lenders will require

[61,484]

> that the cost-revenue stream be fairly predictable. [[37]]

Second, and more fundamentally, capping total revenue recovery for long-term firm transmission service at the cost of expanding the transmission system to alleviate the constraint provides a monetary incentive for FPL to undertake transmission expansion decisions when they are warranted.

In the Policy Order, the Commission concluded that there was no need to cap FPL's legitimate and verifiable opportunity costs for short-term firm transmission service (i.e., less than one year):

> The Commission does not believe that the supply of new capacity will be strategically withheld for the purpose of driving up prices of short-term transmission service, given FPL's commitment to provide firm long-term service at cost-based prices.[[38]]

However, this logic reinforces that timely expansion for long-term firm transmission service requests is absolutely critical. The entire basis for permitting a utility to charge opportunity costs associated with long-term firm transmission service in lieu of expansion costs is that it provides a less expensive method of making transmission capacity available than constructing new facilities. But if expanding the transmission system is the least-cost method to satisfy a request for long-term firm transmission service, clearly FPL should undertake the necessary construction. This is what FPL would do in evaluating its own long-term transmission service needs; comparability dictates that FPL should do no less for third-party wheeling customers. Accordingly, apart from ordinary O&M and line loss revenues, we will not allow FPL to recover revenues from a firm transmission customer associated with long-term firm transmission service which exceed the costs of expanding the system to alleviate the constraint.[[39]]

FPL also seeks clarification of the suggested alternative treatment of opportunity costs. FPL describes its understanding of the "alternative treatment" as follows:

> [U]tilities have the option of identifying all of the legitimate and verifiable opportunity costs that are incurred in operating the transmission system, without seeking to identify which class of customer caused them to be incurred, and to allocate those costs on a *pro rata*, non-discriminatory basis among all classes of transmission customers. Thus, if FPL were periodically required to deviate from the economic dispatch of its generation in order to relieve a transmission constraint, the associated cost would represent an opportunity cost to be allocated among transmission users. Even if this cost would not have been incurred "but for" a certain wheeling transaction, native load and other wheeling customers would be required to bear a *pro rata* share of the cost. And alternatively, even if the cost would have been incurred in the absence of any wheeling transactions, wheeling customers would be required to bear a *pro rata* share of the cost.[[40]]

FPL's interpretation is entirely correct. This form of pricing is permissible because it does not purport to mix embedded cost pricing (which attempts to allocate costs among customers based upon usage) with incremental cost pricing (which attempts to assign costs among users based upon causation). In essence, this "alternative" allows a utility to treat opportunity costs as part of average embedded costs that are equitably allocated among all firm transmission users (native load as well as third party) based upon their collective usage of the transmission system. This approach is fully consonant with the Commission's existing methods of pricing firm transmission service.

Finally, we decline to grant Florida Cities' request, supported by Seminole, that we state that they should not be charged opportunity costs under any circumstances. We did not in our Transmission Pricing Policy Statement, and we will not now, make any generic pronouncement about whether Florida Cities would or would not be liable for opportunity costs in all possible circumstances. We evaluate all proposed rates, including those containing opportunity cost charges, on a case-by-case basis. [41] We do and will continue to determine liability for opportunity costs in each individual case in which the question arises. Because no material issue of fact exists here, [42] we will

[61,485]

reject Florida Cities' alternative request to set the matter for hearing.

Energy Resale Restrictions

Background

In the Policy Order, the Commission ordered FPL to delete from its Rate Schedule PR (Partial Requirements) the provision restricting sales by its Partial Requirements (PR) customers to the economy energy market when FPL's incremental production costs *exceed* its incremental revenues. [43] Because Florida's Energy Broker matches the highest incremental cost resource against the lowest decremental cost resource during any hour, FPL claims that the resale restriction is necessary to ensure that FPL is never required to use high cost resources to displace another utility's lower cost resource. In the Policy Order, the Commission found that the restriction is "overly broad and fails to discriminate between efficient and inefficient trades on the Florida Broker." [44] The Commission acknowledged that the resale of power by FPL's PR customers could result in inefficient trades on the Broker. However, the Commission found that the restriction is "misdirected and too broad" because "[w]hether a resale of PR power on the Broker is efficient or inefficient does not depend on the difference between FPL's incremental production cost and its incremental PR sales revenue, but depends instead on the relationship between FPL's incremental cost and the highest cost resource sold on the Broker." [45]

FPL and the Florida Commission filed requests for rehearing on this issue.

On rehearing, FPL makes three main arguments. First, FPL argues that the Commission apparently incorrectly analyzed the economic effects of deleted section 23(a), and that the Commission fails to recognize the efficiencies that result from the coordinated operations of the Florida Broker. According to FPL, "aside from the individual savings realized by the matching utilities, the overall cost of generating power within the State of Florida is reduced because the lowest incremental cost resources will displace the highest decremental cost resources." [46] In the Policy Order, the Commission considered a hypothetical case in which the highest cost resource used on the Florida Broker is 10 mills, FPL's incremental cost is 8 mills and the PR rate is 6 mills. The Commission found that the restriction would prevent a PR customer from reselling on the Broker (because FPL's incremental cost is greater than the PR rate), even though the reselling would be efficient (because FPL's 8 mill resource would displace a 10 mill resource). FPL argues on rehearing that the restriction would not prevent the efficient trade because FPL would simply make the sale using its 8 mill resource. In addition, FPL argues that allowing a PR customer to quote the 6 mill rate on the Broker when incremental cost is really 8 mills could prevent a more efficient 7 mill resource from making the sale.

Second, FPL argues that removing the restriction would allow PR customers to capture trade gains that should be allocated to all of FPL's customers. When FPL makes an economy sale, FPL's retail and wholesale customers who are paying their share of costs receive their proportionate share of the benefits through revenue credits in formula rates. When a PR customer makes the sale, it claims the entire benefit.

Third, FPL argues that the Commission's suggestion that marginal cost rates would alleviate FPL's concerns without restricting trade [47] is inappropriate. FPL contends that its proposed rates under Schedule PR "reflect FPL's average costs because that rate design is in accordance with the Commission's traditional rate design, as applied to FPL in Opinion No. 57." [48] FPL urges the Commission to confine its review of FPL's proposal to the justness and reasonableness of the proposal itself.

[61,486]

The Florida Commission also makes three main arguments on rehearing. First, the Broker's objective to match trades on the basis of highest incremental cost to lowest decremental cost cannot be achieved by a PR customer reselling because the PR customer does not have an hourly incremental cost when it is using FPL's energy at fixed average embedded cost; rather, the actual cost to produce the energy that is being resold on the Broker during that hour is FPL's incremental cost. Second, PR customers that resell PR energy when PR rates are less than incremental cost do so at the expense of FPL's customers who are paying the difference between the higher incremental costs and the lower average cost rate paid by the PR customer. The Florida Commission agrees with FPL that "absent the resale restriction provision in its proposed tariff, operating costs in Florida will not be reduced as much as they would if proper matches were made through the Broker and there is also the potential for operating costs to increase." [49] Third, referring to the Commission's statement in the Policy Order that FPL is free to propose and support marginal-cost rate designs, the Florida Commission states that it "believes that marginal cost rate design may harm the PR customer's native load, particularly if commingled with embedded cost rates." [50]

Resolution

We will deny rehearing on this issue. We have carefully considered all of the parties' arguments. However, we must view the parties' concerns in light of our statutory obligation to ensure that all rates that we approve are just and reasonable under section 205 of the FPA. We cannot meet that obligation if we approve an overly broad provision restricting the actions of FPL's customers. The Commission continues to find that FPL's proposed restriction is an overly broad way of dealing with the potential problem of inefficient trading by FPL's PR customers. The Commission consistently has rejected resale restrictions as an unnecessarily blunt device, given their potential anticompetitive effects and the availability of other ways to address legitimate utility concerns. [51]

Neither FPL nor the Florida Commission offers any argument on rehearing to persuade us that we have erred. FPL has not demonstrated any overriding public interest considerations in support of the proposed restriction. FPL's concerns stem from the fact that its average cost-based PR energy process may not reflect FPL's incremental costs. The solution to that problem is for FPL to provide PR customers that want to resell resources on the Broker with an appropriate price signal. As we stated in the Policy Order, prohibiting an entire class of transactions is not an appropriate way to resolve that problem.

We have considered FPL's and the Florida Commission's arguments regarding the effects upon efficiency that could result when PR energy that is priced at average cost is resold in the bulk power market. We stress that the restriction as proposed would reach beyond the simple reselling of average cost power. PR customers' resources are not limited to FPL's energy sold under the PR tariff, but include their own generation resources that they either operate or purchase. PR customers use these combined resources to meet their own load and to make sales or purchases on the Broker. Restricting their ability to trade based on the relationship between FPL's incremental cost and its average cost price signal would hamper the PR customers' ability to compete in the market using their own resources. We cannot allow this potential anticompetitive effect to exist, when there is a more precise way to resolve FPL's concerns. FPL remains free to propose in a separate section 205 filing an alternative pricing method for its PR customers.

FPL and the Florida Commission also raise concerns about the Policy Order's suggested alternative of marginal cost-based rates. FPL argues that average cost pricing is in accordance with the Commission's traditional rate design as applied to FPL, and that the Commission's review of FPL's proposal should be limited to the justness and reasonableness of the proposal itself. We agree, and that is what we have done. [52] Our review of that proposal shows that it is unacceptable for the reasons discussed herein.

The Commission does not understand the Florida Commission's specific concern in its argument that a marginal cost rate design may harm the PR customer's native load, especially if commingled with embedded cost rates. We note that utilities with generation resources face hourly incremental energy cost signals. Those costs are taken into account in designing

[61,487]

average cost rates for native load customers. Having the PR customers face an incremental cost energy price signal would not be unusual or necessarily harmful. We again stress, however, that FPL is free to propose any alternative pricing method, or, for that matter, to continue with its average cost based rate design.

We need not address FPL's and the Florida Commission's concerns regarding the allocation of benefits associated with economy energy sales. The source of those concerns is the average cost price signal. FPL can address those concerns itself with the adoption of an appropriate energy price signal.

Divisor for Transmission Rates

Background

In the Policy Order, the Commission ordered FPL to follow the established Commission policy of using the annual system peak (as a proxy for the utility's transmission system capability) as the divisor for non-customer-specific transmission rates. [53]

FPL, Seminole, and Florida Cities request rehearing and/or clarification on this issue. FPL insists that it "need only show that the end-result of its proposal is a just and reasonable rate." [54] FPL contends that the Commission approved the same methodology twelve years ago in a case involving FPL, [55] and that, therefore, we should approve FPL's proposal here. FPL complains that, under the Commission's present methodology, it consistently underrecovers its costs. According to FPL, "If the Commission insists on using system capability as the denominator for non-customer-specific rates, it must exclude from the numerator revenue credits generated from such third-party transmission services in order to treat native load customers fairly and consistently." [56] FPL describes the effect of the Commission's policy as allowing the transmission customer to get the benefits of the 1-CP denominator, keep the revenues it would get from assigning its contracted-for transmission capacity to others, and get a portion of the revenue credits generated by FPL. [57] FPL urges the Commission to explain why this effect would be fair to FPL.

Seminole requests that the Commission clarify that it does not intend to allow utilities to use non-customer-specific rates in all cases. Seminole notes that the FPL filings at issue in this proceeding include "requirements rates containing an approach to transmission cost allocation substantially the same as that contained in the tariffs, as well as certain customer-specific transmission rate schedules, including the Seminole [agreement], which are in fact not comparable to service offered under the proposed tariff. . . ." [58] Seminole states that, because of the load-following nature of some of the services that Seminole gets from FPL, it is essential that FPL derive unit rates for those services "by use of a two-step process consisting of an initial allocation to Seminole of both production and transmission costs on a 12 CP customer-class specific basis, followed by the division of costs so allocated by the billing determinants used specifically with regard to Seminole for the supply of such services." [59]

Florida Cities ask the Commission to include this issue in the ongoing evidentiary hearing. Florida Cities wants the opportunity to show that the divisor should be larger than the annual system peak, even for firm transmission service.

Seminole filed an answer in support of Florida Cities' request for inclusion of this issue in the hearing.

FPL filed an answer to Seminole's and Florida Cities' requests for clarification on this issue. FPL insists that the Commission did not intend to allow parties to address at hearing the question of the appropriate divisor for non-customer-specific rates. FPL also states that it "agrees that the Commission's decision in *Southern* addressed transmission services, not requirements services, and FPL believes that the Commission did not intend to apply the rationale of *Southern* to full and partial requirements services." [60]

Resolution

The Commission will order the presiding administrative law judge to include in the ongoing hearing proceeding the issue of whether a number other than annual peak could be justified as a divisor for non-customer-specific transmission rates. We have acknowledged that the annual system peak may not necessarily be the only denominator that will produce just

[61,488]

and reasonable rates. In *AEP*, issued after the date of issuance of the Policy Order, we explained:

> [W]e have used annual transmission system peak as a proxy for system capability because it reflects the demonstrated capability of the transmission system and it is a figure that is readily available. The intervenors may, however, argue in support of other measures of system capability during the hearing if they wish to do so.[[61]] Additionally, in the Transmission Pricing Policy Statement, we stated:
>
> The Commission concludes that greater pricing flexibility is now required for several reasons. First, exclusive use of methods that worked reasonably well in the past does not provide sufficient flexibility to accommodate the evolving needs of transmission owners and users in a more competitive era. It is important to gain practical experience with alternative transmission pricing approaches in order to assess how best to accommodate the current and future needs of the industry in providing efficient and reliable power supply as the industry becomes increasingly competitive.[[62]]

Accordingly, we believe that it is appropriate to allow the parties at hearing to pursue the issue of whether the proxy number for system capability should be a different number than the transmission system's annual system peak.

Concerning Seminole's remaining request for clarification, [63] we clarify that our discussion of this issue is *not* intended to apply to FPL's customer-specific rate schedules in this proceeding. Seminole is correct that the Policy Order, June 16 Order, and August 4 Order do *not* hold that non-customer specific rates automatically would be considered just and reasonable if applied to services that FPL provides on a customer-specific basis.

B. *The June 16 Order Rehearings*

We will deny FPL's and Tampa's requests for rehearing of the June 16 Order. FPL and Tampa have presented nothing new on rehearing to convince us that we erred in setting for hearing the *Mobile-Sierra* issue. Moreover, we are satisfied that we have sufficiently defined the scope of the evidentiary hearing on the comparability issue. Consistent with our direction on the subject in *AEP*, we leave it to the presiding judge to determine what submissions the parties should make in order to create a factual record that ultimately will enable the Commission to ascertain whether FPL's tariffs actually do provide comparable service (or, if not, exactly what modifications should be made).

Concerning Tampa's request that the Commission now order FPL to apply the same rates, terms and conditions of service contained in its filed transmission tariffs to itself in making wholesale power sales, we decline to make such a broad order at this time in this proceeding. Any wholesale power sales will necessarily come before this Commission, and at that time we will consider whether such power sales as proposed meet the *AEP* comparability standard. Tampa has not justified the need for interim relief.

C. *The August 4 Order Rehearing*

We will deny FPL's request for rehearing of the August 4 Order. FPL has not presented sufficient reason to upset our prior decision in the August 4 Order (relying in part on our decision in the June 16 Order) to set the contested *Mobile-Sierra* issue for hearing. We continue to believe, based on the parties' pleadings, that it is not clear whether FPL has the unilateral authority to file the proposed rate changes. We find that an evidentiary hearing is the appropriate forum for the resolution of this particular contract interpretation question.

As we stated in the June 16 order, "We believe that the arguments presented by the parties on Florida Cities' *Mobile-Sierra* issue raise a question of fact concerning the parties' intentions that we are unable to resolve at this time." [64] We continue to believe that this is the proper procedure. FPL's repeated arguments do nothing to answer the questions of fact--those are for the evidentiary hearing.

The Commission orders:

The requests for rehearing and/or clarification of FP&L, Seminole, Florida Commission, Tampa, and Florida Cities are hereby granted

[61,489]

in part and denied in part, as discussed in the body of this order.

Commissioner Hoecker *concurred* with a separate statement attached.

James J. HOECKER, Commissioner, *concurring*:

Consensual decisionmaking seldom yields perfection; so, today I join my colleagues in voting for a good change in policy, although an arguably better end result is readily available. I concur that utilities proposing to charge opportunity cost rates for long-term transmission service (under the Commission's "or" pricing policy [1]) should compute the increment of costs associated with foregone business opportunities on a basis other than life-of-the-transaction. While that approach restrains rates based on "or" pricing, it entails undue administrative burdens. Today we instruct utilities to measure the difference between embedded and opportunity costs on a one-year period. This approach is simple and can be said to correspond to fiscal year accounting or a 12-month "test period" for establishing rates. I nevertheless believe that it may be more reasonable for utilities to calculate opportunity costs in accordance with their individual planning horizons or construction cycles, whatever that might be. The reasons for this are straightforward.

Although calculating opportunity costs on an annual basis avoids the potential revenue impacts produced by Florida Power & Light Company's "hourly" methodology and tends to prevent new customers from being trapped "at the margin" indefinitely, it is not flexible, reflects no particular ratemaking practice (except insofar as utility books of account track fiscal years), and bears no relationship to the objectives of the Commission's transmission pricing policy statement. [2]

The planning horizon approach, on the other hand, achieves the first two results and is also consistent with the Commission's transmission pricing policy in at least two important respects. First, the Commission's policy statement indicated that *transmission pricing must reflect comparability.* From the perspective of a transmission-owning utility, expansion of the transmission system to meet the needs of its native load customers makes economic sense only if, over its planning horizon, opportunity costs due to a transmission constraint exceed the cost of constructing additional facilities to alleviate the constraint. If a utility were required to use the planning horizon that it employs to plan its capital requirements to also calculate opportunity costs associated with third party transmission requests, that utility would then be basing the opportunity cost portion of third party transmission rates on the same cost projection horizon that governs its decisions to invest in its transmission system to serve its own needs. Because opportunity costs are capped at the costs necessary to expand the system to alleviate the constraints associated with a "lost opportunity," [3] the needs of third party transmission customers receive the same cost recognition as the needs of the utility's native load customers. It is my understanding that no utility projects its investment needs on an annual basis.

Second, the Commission concluded that *transmission pricing should be practical.* I can think of no more practical or flexible approach than allowing individual utilities to make opportunity costs calculations utilizing the same timeframe they employ to plan their systems. The revenue cap requirement (which is still computed on a life-of-the-transaction basis) implicitly requires a utility charging opportunity costs to look to its planning horizon as a practical means of demonstrating the projected cost of alleviating the constraint that gives rise to foregone revenues. The Commission's task of reviewing those cost projections is also made easier and less controversial because it is not looking at annualized costs for one purpose and longer term planned investments for another.

I will be interested to see if these concerns resonate on rehearing.

-- Footnotes --

[61,478]

[1] *See Florida Power & Light Company*, 66 FERC ¶61,227 (1994) (Policy Order), *reh'g pending*; *Florida Power & Light Company*, 67 FERC ¶61,326 (1994) (June 16 Order), *reh'g pending*; *Florida Power & Light Company*, 68 FERC ¶61,214 (1994) (August 4 Order), *reh'g pending.* In addition to the three orders pending on rehearing here, the Commission also has issued other orders (responding to additional FPL filings or customer complaints) consolidating this proceeding with the related proceedings in Docket Nos. ER93-922-000, ER93-507-000, EL93-28-000, and EL93-40-000, EL94-12-000, EL94-28-000, and EL94-47-000. *See Florida Power & Light Company*, 65 FERC ¶61,155 (1993), *order on reh'g*, 68 FERC ¶61,214 (1994); *Florida Power & Light Company*, 65 FERC ¶61,284 (1993), *reh'g denied*, 67 FERC ¶61,141 (1994); *Seminole Electric Cooperative, Inc. v. Florida Power & Light Company, et al.*, 65 FERC ¶61,413 (1993), *reh'g denied*, 66 FERC ¶61,229 (1994); *Seminole Electric Cooperative, Inc. v. Florida Power & Light Company, et al.*, 69 FERC ¶61,011 (1994).

[2] *Florida Power & Light Company*, 64 FERC ¶61,361 (1993) (September 24 Order), *order on reh'g*, 67 FERC ¶61,326 (1994) (June 16 Order), *reh'g pending.*

[3] 64 FERC at p. 63,486.

[4] *Florida Power & Light Company*, 67 FERC ¶61,326 (1994) (June 16 Order), *reh'g pending.*

[5] The particulars of FPL's filing are described at length in the underlying orders and will therefore not be repeated here.

[6] *Florida Power & Light Company*, 66 FERC ¶61,227 (1994) (Policy Order), *reh'g pending.*

[61,479]

[7] Florida Cities are comprised of the Florida Municipal Power Agency (FMPA), Gainsville Regional Utilities, and the Cities of Fort Pierce, Homestead, Key West, Kissamee, Lakeland, Lake Worth, St. Cloud, Starke, and Vero Beach, Florida.

[8] *See United Gas Pipe Line Company v. Mobile Gas Service Corporation*, 350 U.S. 332 (1956); *FPC v. Sierra Pacific Power Company*, 350 U.S. 348 (1956).

[9] The Commission later issued proposed and final orders in this related proceeding in Docket Nos. EL93-51-000 and TX93-4-000, in *Florida Municipal Power Agency v. Florida Power & Light Company*, 65 FERC ¶61,125 (1993) (*proposed order*), and 67 FERC ¶61,167 (1994) (*final order*), *reh'g pending.*

[10] 67 FERC ¶61,168, *clarified*, 67 FERC ¶61,317 (1994) (*AEP*).

[11] *See* 65 FERC at p. 61,762.

[12] *See* 67 FERC at pp. 62,148-49.

[61,480]

[13] *Florida Power & Light Company*, 68 FERC ¶61,214 (1994) (August 4 Order), *reh'g pending.*

[14] *See Florida Power & Light Company*, 65 FERC ¶61,155 (1993).

[15] *See also Inquiry Concerning the Commission's Pricing Policy For Transmission Services Provided by Public Utilities Under the Federal Power Act, Policy Statement*, 59 Fed. Reg. 55031 (1994), 69 FERC ¶61,086 (1994) (*Transmission Pricing Policy Statement*).

[16] FPL September 6 Rehearing at p. 2.

[17] FPL September 6 Rehearing at p. 1. In the June 16 Order, the Commission stated that “Seminole’s argument (to the extent the Commission understands it) is that FPL’s proposed requirements and interchange formula rates must be rejected on *Mobile-Sierra* grounds because FPL failed to seek a specific waiver to change from stated to formula rates.” 67 FERC at p. 62,149.

[18] FPL September 6 Rehearing at p. 17.

[19] 18 C.F.R. §35.1(d)(2) (1994). That regulation provides a paragraph that must be included in certain rate schedules when the contracting parties intend that the party furnishing service shall have the unrestricted right to file unilateral rate changes under section 205 of the FPA. We note that the FPL-Seminole agreements cited by FPL do not contain the precise language specified in section 35.1(d)(2) of the Commission’s regulations.

[61,481]

[20] 61 FERC ¶61,009 (1992), *reh’g pending.*

[21] 66 FERC at p. 61,525 and n.10, *citing Pennsylvania Electric Company v. FERC*, 11 F.3d 207 (D.C. Cir. 1993) (*Penelec*).

[22] 66 FERC at p. 61,525.

[23] 65 FERC ¶61,153 (1993).

[24] 66 FERC at p. 61,526.

[25] FPL Rehearing at p. 6.

[26] FPL Rehearing at p. 7.

[27] FPL Rehearing at p. 7, *citing New England Power Company and Northeast Utilities Service Company*, 61 FERC ¶61,009, at p. 61,060 (1992).

[28] Florida Cities Rehearing at p. 2.

[61,482]

[29] *See* 58 FERC ¶61,069, at p. 61,179 (1992), *reh’g pending.*

[30] The “discount” may be either in the form of a reduced rate per unit of service or in the form of only having to pay for service in those hours in which service is taken.

[31] *See New England Power Company*, Opinion No. 335, 49 FERC ¶61,129 (1989), *reh’g denied*, Opinion No. 335-A, 50 FERC ¶61,151 (1990), *aff’d*, No. 90-1179 (D.C. Cir. Feb. 11, 1991) (unpublished).

[32] 66 FERC at p. 61,526.

[61,483]

[33] With regard to transactions under FPL’s Transmission Tariff No. 2, under which customers may enter into transactions with durations ranging from one day to one year, the Commission continues to believe that a life-of-transaction comparison is necessary and appropriate.

[34] Eliminating the uncertainty of future refunds should, all things being equal, reduce the utility's risk and hence its cost of capital over time. This would, of course, benefit consumers.

[35] *Northeast Utilities Service Company (Re: Public Service Company of New Hampshire)*, 62 FERC ¶61,294, at p. 62,926 (1993), *reh'g pending.*

[36] *See generally* 18 C.F.R. §35.13 (1994).

[61,484]

[37] 64 FERC ¶61,279, at p. 62,976 (1993).

[38] 66 FERC at p. 61,527.

[39] Where construction costs exceed the original expansion cost estimate due to major unforeseen events which are beyond the control of the utility, the utility may seek to revise the cost cap through an appropriate filing under section 205. *See Northeast Utilities Service Company (Re: Public Service Company of New Hampshire)*, 56 FERC ¶61,269, at p. 62,032 (1991).

[40] FPL Rehearing at p. 11.

[41] *See Northeast Utilities Service Company v. FERC*, 993 F.2d 937, 957 (1st Cir. 1993), *citing* 58 FERC at p. 61,204 and n.118.

[42] In this regard, we remain unconvinced that the licensing conditions imposed by the Nuclear Regulatory Commission bar opportunity cost pricing to Florida Cities (or other similarly-situated customers). The licensing conditions cited by Florida Cities (St. Lucie conditions) do not address opportunity cost pricing.

[61,485]

Rather, as recognized by Florida Cities, these conditions explicitly allow the recovery of all reasonable costs of transmission. Opportunity costs as allowed here are, by definition, reasonable costs of transmission. Florida Cities have not cited any other language in the licensing conditions that compels a different conclusion, and remaining references to FPL's actions in implementing the conditions and planning and operating its system are not sufficient to overcome our general policy, explained above, concerning opportunity cost pricing.

[43] Section 23(a) of Rate Schedule PR provided that a PR customer may resell energy purchased under the PR Rate Schedule to a third party pursuant to an economy energy sale, a coordination sale, or a similar transaction in any hour during which FPL's incremental energy cost for the affected power is expected to be *equal to* or *less than* the incremental energy revenue received under the PR Rate Schedule in connection with FPL's sale of such power to the PR customer. FPL Rehearing at p. 12.3.

[44] 66 FERC at p. 61,528. The Florida Broker is a trade mechanism for economy energy transactions in peninsular Florida. *See* 66 FERC at p. 61,527 and n.22.

[45] 66 FERC at p. 61,528.

[46] FPL Rehearing at p. 13.

[47] *See* 66 FERC at p. 61,529 and n.29.

[48] FPL Rehearing at pp. 17-18 (footnotes omitted).

[61,486]

[49] Florida Commission Rehearing at p. 3.

[50] *Id.* at pp. 3-4.

[51] *See Gulf States Utilities Company*, 5 FERC ¶61,066 (1978); *Northern Indiana Public Service Company*, 23 FERC ¶61,249, at p. 61,538 (1983); *Ohio Edison Company*, 43 FERC ¶61,316 (1988); *Missouri Public Service Company*, 54 FERC ¶61,357, at p. 62,177 (1991); and *Georgia Power Company*, 63 FERC ¶61,269, at p. 62,732 (1993).

[52] We note that our current policy is that transmission rates, to the extent practicable, should be designed to reflect marginal costs. Transmission Pricing Policy Statement, slip op. at p. 20.

[61,487]

[53] 66 FERC at p. 61,529, *citing Southern Companies Services, Inc.*, 61 FERC ¶61,339 (1992), *reh'g denied*, 63 FERC ¶61,217 (1993) (*Southern*).

[54] FPL Rehearing at p. 19 (footnote omitted), *citing FPC v. Hope Natural Gas Company*, 320 U.S. 591, 602 (1944).

[55] FPL Rehearing at pp. 22-23, *citing Florida Power & Light Company*, Opinion No. 152, 21 FERC ¶61,070 (1982), *reh'g denied*, Opinion No. 152-A, 22 FERC ¶61,012 (1983).

[56] FPL Rehearing at p. 27.

[57] FPL Rehearing at p. 27.

[58] Seminole Rehearing at p. 10.

[59] Seminole Rehearing at p. 5.

[60] FPL April 12 Answer at p. 6; *see supra* note 44 (citing *Southern*).

[61,488]

[61] 67 FERC at p. 61,488, *citing American Electric Power Service Corporation*, 64 FERC ¶61,279 (1993) (footnote omitted).

[62] Transmission Pricing Policy Statement, slip op. at pp. 8-9. While the Policy Statement does not apply to FPL's filings in this proceeding (FPL made its filings before the Policy order issued), it does reflect the Commission's current commitment, demonstrated in *AEP*, to increased pricing flexibility (if properly supported).

[63] Seminole also filed a second request for clarification (of all three orders) on August 12, 1994, which expresses substantially the same concerns as its March 28, 1994 request for clarification of the Policy Order.

[64] 67 FERC at p. 62,149.

[61,489]

[1] *Northeast Utilities Service Company*, Opinion No. 364-A, 58 FERC ¶61,070 (1992).

[2] *FERC Statutes and Regulations* ¶31,005 (1994).

[3] *Pennsylvania Electric Company*, 58 FERC ¶61,278, at p. 61,874 (1992).