

134 FERC ¶ 61,044
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Marc Spitzer, Philip D. Moeller,
John R. Norris, and Cheryl A. LaFleur.

California Public Utilities Commission

Docket No. EL10-64-002

Southern California Edison Company
Pacific Gas and Electric Company
San Diego Gas & Electric Company

Docket No. EL10-66-002

ORDER DENYING REHEARING

(Issued January 20, 2011)

1. On October 21, 2010, the Commission issued an order granting the California Public Utilities Commission's (CPUC) request for clarification,¹ and dismissing rehearing, of the July 15, 2010 order addressing the CPUC's petition for declaratory order and the separate petition for declaratory order filed by Pacific Gas and Electric Company (PG&E), Southern California Edison Company (SCE), and San Diego Gas & Electric Company (SDG&E) (collectively, Joint Utilities).² On November 22, 2010, the Joint Utilities filed a request for rehearing, or, in the alternative, reconsideration, partial vacatur, or clarification of the Clarification Order, and the Edison Electric Institute (EEI) filed a request for rehearing of the Clarification Order.

2. In this order, the Commission denies rehearing of the Clarification Order, as discussed below.

¹ *California Public Utilities Commission*, 133 FERC ¶ 61,059 (2010) (Clarification Order).

² *California Public Utilities Commission*, 132 FERC ¶ 61,047 (2010) (July 15 Order).

I. Background

3. The CPUC's petition for declaratory order, submitted on May 4, 2010 in Docket No. EL10-64-000, requested that the Commission find that sections 205 and 206 of the Federal Power Act (FPA),³ and section 210 of the Public Utility Regulatory Policies Act of 1978 (PURPA)⁴ and Commission regulations do not preempt the CPUC's decision to require California utilities to offer a certain price to combined heat and power (CHP) generating facilities of 20 MW or less that meet energy efficiency and environmental compliance requirements. The Joint Utilities filed a separate petition for declaratory order on May 11, 2010, in Docket No. EL10-66-000, in which they argued that the CPUC's decision is preempted by the FPA insofar as it sets rates for electric energy that is sold at wholesale.

4. The California "Waste Heat and Carbon Emissions Reduction Act," Assembly Bill (AB) 1613, amended the California Public Utilities Code to require "electrical corporations" in California (i.e., investor-owned utilities (IOU) regulated by the CPUC) to offer to purchase, at a price to be set by the CPUC, electricity that is generated by certain CHP generators and delivered to the grid.⁵ CHP generators eligible for the price set by the CPUC must have a generating capacity of not more than 20 MW and must meet certain efficiency and emissions standards. The legislation requires CPUC-jurisdictional utilities to file standard ten-year purchase contracts (AB 1613 feed-in tariffs) with the CPUC that require them to offer to purchase at the CPUC-set price electricity generated by eligible CHP generators. As amended, the California Public Utilities Code states that this tariff shall "provide for payment for every kilowatt hour delivered to the electrical grid by the combined heat and power system at a price determined by the commission."⁶ AB 1613 requires that the CPUC set the rates at which the utilities must offer to purchase from CHP generators at a level that "ensure[s] that ratepayers not utilizing [CHP] systems are held indifferent to the existence of [the AB 1613 feed-in] tariff."⁷

³ 16 U.S.C. §§ 824d, 824e (2006).

⁴ 16 U.S.C. § 824a-3 (2006); *see generally* 16 U.S.C. § 2601 *et seq.* (2006).

⁵ CPUC May 4, 2010 Petition at 2-3.

⁶ Cal. Pub. Util. Code § 2841(b)(2) (2010). The term "the commission" in the California Public Utilities Code refers to the CPUC.

⁷ *Id.* § 2841(b)(4).

5. The July 15 Order found that the CPUC's decision to require California utilities to offer a certain price to CHP generating facilities of 20 MW or less that meet energy efficiency and environmental compliance requirements would not be preempted by the FPA, PURPA, or Commission regulations, as long as the program meets certain requirements. The Commission explained that a state commission may, pursuant to PURPA, determine avoided cost rates for qualifying facilities (QF). The Commission found that, although the CPUC did not argue that its AB 1613 program is an implementation of PURPA, to the extent the CHP generators that can take part in the AB 1613 program obtain QF status pursuant to the Commission's regulations, the AB 1613 feed-in tariff would *not* be preempted by the FPA, PURPA, or Commission's regulations⁸ as long as: (1) the CHP generators from which the CPUC is requiring the Joint Utilities to purchase energy and capacity are QFs pursuant to PURPA; and (2) the rate established by the CPUC does not exceed the avoided cost of the purchasing utility.⁹

6. The CPUC sought clarification of the July 15 Order, requesting clarification that the CPUC could implement AB 1613 pursuant to the provisions of PURPA by explicitly setting new avoided cost rates using a multi-tiered avoided cost rate structure. The CPUC requested clarification that: (1) the CPUC can require retail utilities to consider, in the avoided cost calculation, factors that promote development of more efficient CHP facilities; and (2) "full avoided cost" need not be the lowest possible avoided cost and can properly take into account real limitations on "alternate" sources of energy imposed by state law. The CPUC also requested that the Commission clarify that, for CHP systems located in transmission-constrained areas, a permissible component of avoided cost consideration could be a 10 percent price "adder" to reflect the avoided costs of the construction of distribution and transmission upgrades that would otherwise be needed.

7. The Clarification Order granted the CPUC's request for clarification by explaining that the conceptual framework discussed in the CPUC's request for clarification is consistent with the avoided cost requirements in section 210 of PURPA. The Commission found that the concept of a multi-tiered avoided cost rate structure can be consistent with the avoided cost rate requirements set forth in PURPA and its regulations.¹⁰ With respect to the "adder" for CHP systems located in transmission-constrained areas to reflect the avoided costs of the construction of distribution and transmission upgrades that would otherwise be needed, the Commission explained that, if

⁸ July 15 Order, 132 FERC ¶ 61,047 at P 65 (citing 18 C.F.R. § 292.101 *et seq.* (2010)).

⁹ *Id.* P 67 (citing 18 C.F.R. § 292.304 (2010)).

¹⁰ Clarification Order, 133 FERC ¶ 61,059 at P 26 (citing 16 U.S.C. §§ 824a-3(a), (b),(d) (2006), and 18 C.F.R. §§ 292.101(b)(6), 292.304(a) (2010)).

the CPUC bases the avoided cost “adder” on an actual determination of the expected costs of upgrades to the distribution or transmission system that the QFs will permit the purchasing utility to avoid, such an “adder” would constitute an actual avoided cost determination and would be consistent with PURPA and our regulations.¹¹

8. The Commission also explained that, in the July 15 Order, it did not rule whether the rates established by the CPUC to implement its AB 1613 program would either satisfy or violate the avoided cost rate requirements set forth in section 210 of PURPA and the Commission’s regulations, and that it did not rule in the July 15 Order, and was not ruling in the Clarification Order, whether the CPUC’s offer price is consistent with the avoided cost rate requirements of PURPA.¹² In both the July 15 Order and the Clarification Order, the Commission explained that there was no record in these proceedings on which the Commission could determine whether the CPUC’s offer price under its AB 1613 program was, in fact, consistent with the avoided cost rate requirements of section 210 of PURPA.¹³

II. Requests for Rehearing

9. The Joint Utilities and EEI object to the Commission’s determination in the Clarification Order that the concept of a multi-tiered avoided cost rate structure can be consistent with the avoided cost rate requirements set forth in PURPA and the Commission’s regulations.¹⁴

10. The Joint Utilities argue that the Commission should vacate portions of the Clarification Order because it addresses an issue that was not before the Commission, was not briefed, and that is not relevant to the AB 1613 program. According to the Joint Utilities, neither AB 1613 nor the AB 1613 decisions, nor anything else in California law imposes a requirement that electrical corporations purchase any particular percentage of their energy needs from CHPs satisfying the requirements for participation in the AB 1613 program. The Joint Utilities assert that, in addressing the question of whether states may create a multi-tiered avoided cost rate structure based on requirements that a utility

¹¹ *Id.* P 31.

¹² *Id.* P 25 (citing July 15 Order, 132 FERC ¶ 61,047 at P 68).

¹³ *Id.*

¹⁴ EEI endorses the request for rehearing and other relief filed by the Joint Utilities. EEI states that, rather than repeating the arguments in the Joint Utilities’ request for rehearing, it incorporates those arguments into its request for rehearing by reference. EEI Rehearing Request at 6.

purchase a certain percentage of its energy needs from generators with particular characteristics, the Commission did not answer the question framed by the CPUC, namely “whether [the CPUC] may implement a two-tiered rate structure, where AB 1613-compliant QFs receive rates based on higher, long-run avoided cost rates reflecting more stringent efficiency standards, and non-AB 1613 compliant QFs continue to receive rates based on short-run avoided costs.”¹⁵

11. The Joint Utilities further argue that, under the circumstances presented by the AB 1613 program, where one category of CHP does not enable a utility to avoid greater costs by purchasing from it instead of another category of CHPs, the Commission should have made clear that its regulations do not permit a state to discriminate between such categories of CHPs by creating different avoided cost rates. As an example, the Joint Utilities argue that, if it is assumed that a utility avoids the same costs whether it purchases from one category of QFs or another category, and the state requires the utility to pay avoided cost rates for energy and capacity from QFs in the first category, and higher rates for purchases of energy and capacity from QFs in the second category, then the price paid to QFs in the second category exceeds the utility’s avoided cost.¹⁶ The Joint Utilities also argue that PURPA is violated where a program requires utilities to pay a higher price for energy and capacity from more efficient QFs than the avoided cost rate applicable to purchases from QFs that are less efficient because the rate for more the more efficient QFs would necessarily exceed the utility’s avoided cost.¹⁷ According to the Joint Utilities, under the CPUC’s AB 1613 program, a utility would be required to pay one price to a CHP that satisfies all requirements for participation in the AB 1613 program, and a lesser price to a CHP that is comparable in all respects except that it commenced operation before January 2008. The Joint Utilities contend that the CPUC is seeking to establish two concurrent long-term avoided cost formulas, one for QFs that satisfy the efficiency requirements of the AB 1613 program, and another for those that do not.¹⁸

12. The Joint Utilities argue that, although AB 1613 requires the CPUC to ensure that ratepayers not utilizing CHP systems are held indifferent to the existence of the AB 1613 tariff, the CPUC has not interpreted this requirement as the equivalent of a directive requiring it to set the price at the buyer’s avoided cost, but rather the CPUC erroneously

¹⁵ Joint Utilities Request for Rehearing or Clarification at 10-11 (quoting Clarification Order, 133 FERC ¶ 61,059 at P 21).

¹⁶ *Id.* at 12.

¹⁷ *Id.* at 13.

¹⁸ *Id.* at 14.

concluded that ratepayer indifference would be maintained if the price included costs reflecting societal and environmental benefits provided by eligible CHP systems. Further, the Joint Utilities argue that the environmental attributes of a QF and the societal benefits it provides are not a proper factor in the calculation of avoided cost because avoided cost payments are only designed to compensate QFs for the energy and capacity they provide, and must be based solely on the cost the utility avoids by purchasing from QFs.¹⁹ The Joint Utilities also argue that the role of states in setting rates is limited, and that the Commission has already identified a number of ways states may pursue their policy choices and encourage development of particular types of generating facilities consistent with the requirements of PURPA.²⁰

13. The Joint Utilities argue that no notice was provided to the public that avoided cost pricing and/or the effect of purchase mandates on such prices would be the subject of this case. The Joint Utilities contend that both the petitions for declaratory order addressed a non-PURPA program that involved only a general mandate to purchase excess energy from eligible CHPs, and therefore the public was provided no notice that the Commission might rule on how avoided costs are to be calculated under PURPA, or how a state purchase mandate might impact that calculation. The Joint Utilities argue that the Commission's notices in this proceeding do not satisfy the purpose for notices because the notices indicated the issue would be whether a CPUC program that resulted in the setting of wholesale rates was preempted by the FPA, PURPA, and Commission regulations concerning QFs. According to the Joint Utilities, the 49 other state commissions and the utilities required to purchase QF power had no notice that this case might set new precedent on how avoided costs could be calculated.²¹

14. The Joint Utilities also argue that the Commission should grant rehearing of the Clarification Order because its ruling that ““where a state requires a utility to procure a certain percentage of energy from generators with certain characteristics, generators with those characteristics constitute the sources that are relevant to the determination of the utility's avoided cost for that procurement requirement”” is inconsistent with PURPA, the Commission's regulations and applicable precedent. The Joint Utilities contend that limiting the sources that may be considered in setting the avoided cost will result in higher rates that violate PURPA's ratepayer indifference standard, and argue that a decision to require ratepayers to subsidize certain types of favored QFs through the purchase of energy and capacity must be made by Congress through amendments to

¹⁹ *Id.* at 15.

²⁰ *Id.* at 29-30.

²¹ *Id.* at 15-16.

PURPA.²² The Joint Utilities state that, while they agree with the general proposition that “regardless of how the state determines avoided cost, it must in its process reflect prices available from all sources able to sell to the utility whose avoided cost is being determined,” they “do not agree that it follows from this proposition that if the state requires a utility to purchase a certain percentage of its energy needs from generators with certain characteristics, they become the only source relevant to determining avoided costs for that segment of the utility’s requirements.”²³

15. The Joint Utilities argue that the Commission’s holding renders meaningless the PURPA requirement that the rate for QF energy and capacity may not exceed the “incremental cost to the electric utility of alternative electric energy”²⁴ because it would effectively eliminate other sources from the determination of the cost of alternative electric energy. The Joint Utilities also contend that requiring a utility to purchase a specific percentage of its needs from a very narrowly defined category of energy producers would exclude any other lawful sources of energy and capacity from the avoided cost calculation, thereby allowing generators to drive up the mandatory purchase price for their resources because the avoided cost of purchasing from a preferred resource would become the cost of building or purchasing that particular resource.²⁵

16. The Joint Utilities assert that the Commission’s approach is inconsistent with the requirement that its pricing rules must be just and reasonable to ratepayers, and Congress’s intent that utility customers be financially indifferent concerning whether the utility purchases power from a QF, purchases it from another source, or generates the power itself.²⁶ They argue that the Clarification Order invites the states to seek to advance environmental and other goals by disguising subsidies to favored technologies as wholesale power prices, and that ratepayers will no longer be indifferent to the source of power because the utility’s avoided cost would simply be the cost to purchase from, or build, a particular type of preferred generator. The Joint Utilities also argue that excluding from consideration sources of power a utility would rely upon if it did not purchase from certain QFs pursuant to a state mandate results in a rate in excess of avoided cost, and that this undoes the balance struck by Congress in PURPA and by the Commission in its regulations between encouraging QFs and ensuring ratepayers are

²² *Id.* at 17.

²³ *Id.* at 18 (emphasis in original).

²⁴ *Id.* at 19.

²⁵ *Id.*

²⁶ *Id.* at 20.

charged reasonable rates.²⁷ They also contend that this exclusion is inconsistent with the plain language of the Commission's avoided cost regulations,²⁸ and that any differentiation by technologies is subject to the requirement that a utility may not be required to pay more than its avoided cost.²⁹

17. The Joint Utilities also contend that the Commission erred in interpreting *SoCal Edison* as supporting the proposition that ““where a state requires a utility to procure a certain percentage of energy from generators with certain characteristics, generators with those characteristics constitute the sources that are relevant to the determination of the utility's avoided cost for that procurement requirement””³⁰ because this interpretation effectively overrules a key finding in that case. They argue that, in *SoCal Edison*, the Commission held that the CPUC's process of determining avoided costs did not comply with PURPA because it excluded other potential sources of capacity,³¹ and they therefore conclude that *SoCal Edison*, which the Commission has cited with approval a number of times, is inconsistent with the Commission's Clarification Order.³² The Joint Utilities also argue that *Signal Shasta Energy Co., Inc.* does not support the finding in the Clarification Order that a state may appropriately recognize procurement segmentation by making separate avoided cost calculations.³³ The Joint Utilities contend that the Commission did not consider the segmentation of avoided cost in accordance with resource category in *Signal Shasta*, but rather described certain standard offers without expressing approval or disapproval of how the CPUC determined the energy and capacity prices.

18. The Joint Utilities argue that the Commission did not engage in reasoned decision making when it adopted new law and policy without considering a wide variety of ramifications. They argue that there was no opportunity for the Commission to receive the input of interested parties because it did not act through a rulemaking, and that, in this

²⁷ *Id.* at 22.

²⁸ *Id.* at 23 (citing 18 C.F.R. § 292.304(a)(2) (2010)).

²⁹ *Id.*

³⁰ *Id.* at 24 (quoting Clarification Order, 133 FERC ¶ 61,059 at P 27).

³¹ *Id.* at 27.

³² *Id.* at 27-28.

³³ *Id.* at 28 (citing *Signal Shasta Energy Co., Inc.*, 41 FERC ¶ 61,120, at n.4 (1987) (*Signal Shasta*)).

case, a rulemaking is more appropriate to effect the change to the law.³⁴ The Joint Utilities also assert that the CPUC's November 16, 2010 proposed decision to implement the AB 1613 program based on the pricing formula the CPUC had mandated in its AB 1613 decisions demonstrates that there is confusion concerning the Clarification Order.³⁵ The Joint Utilities argue that various related questions of interpretation should be answered before states attempt to implement the Clarification Order.³⁶

19. EEI requests that the Commission revisit the portion of the order in which it provided guidance to the CPUC as to the interpretation and application of the concept of "avoided cost" under PURPA, and either withdraw that guidance, or recognize that the guidance is advisory, does not constitute final agency action and will be subject to further review in individual future proceedings.³⁷ EEI specifically objects to "the portion [of the order] that allows states to set avoided cost rates by type of QF if a state has mandated that a utility purchase a certain percentage of energy from generators that fall within such category."³⁸ EEI contends that this issue is not even before the Commission in these proceedings, and argues that the Clarification Order can be read to give states very wide latitude in setting avoided costs without regard to the potential cost consequences.

20. EEI contends that the holding in the Clarification Order allowing states to limit the sources considered in calculating avoided cost effectively undermines the PURPA requirements that: (1) the cost for purchases of energy by utilities from QFs is not to exceed the purchasing utility's avoided cost; and (2) the rates charged by QFs must be just and reasonable. EEI argues that the Clarification Order allows states to set separate avoided costs for separate categories of QFs, thereby causing higher prices for QF generators than those allowed under the traditional understanding of avoided cost, and in turn raising customer rates.³⁹ EEI also argues that the Clarification Order departs from Congress's intent in PURPA "to protect ratepayers from increases in costs while promoting purchases from QFs."⁴⁰ EEI asserts that the Commission's finding that the concept that separate avoided cost rates for separate categories of QFs could be consistent

³⁴ *Id.* at 32.

³⁵ *Id.* at 9, 32.

³⁶ *Id.* at 31-32.

³⁷ EEI Rehearing Request at 16-17.

³⁸ *Id.* at 3-4.

³⁹ *Id.* at 7-8.

⁴⁰ *Id.* at 8.

with avoided cost requirement under PURPA will permit the avoided cost rate to be set higher than PURPA and Commission precedent allow.⁴¹ According to EEI, the order “narrows the ‘markets’ involved, by allowing states to focus on individual preferred categories of QFs rather than all suppliers in the energy and capacity markets.”⁴² EEI argues that this will place upward pressure on customer rates because the narrower markets will have fewer competitors and more constrained supply.

21. EEI asserts that the Clarification Order departs from the Commission’s traditional interpretation of PURPA “avoided cost” as the cost of alternative energy available to the utility without regard to the technology, size or efficiency of the QF. EEI argues that the Commission’s PURPA implementing regulations have traditionally been understood to mean that, in setting avoided cost rates, states look at the cost of alternative energy available to the purchasing utility without regard to type of QF generator, while taking into account factors such as deliverability and usefulness of the QF energy and impacts on consumer rates.⁴³ EEI asserts that, by allowing states to set avoided costs for categories of a QF generator, the Clarification Order departs from the traditional focus on the cost of alternative energy without regard to energy type.⁴⁴

22. EEI contends that the Commission provided guidance in the Clarification Order without a concrete proposal or underlying record because the CPUC has not engaged in a PURPA avoided cost analysis. EEI asserts that, as a result, the Commission failed to provide adequate notice and opportunity for input by utilities and the public, in contravention of the Administrative Procedure Act and due process requirements. EEI therefore argues that the Commission should withdraw the avoided cost provisions in the Clarification Order and await a concrete proposal that can form the basis for a more informed decision in a future proceeding, with adequate opportunity for comment.⁴⁵

23. EEI also contends that the Clarification Order raises concerns about utilities being locked into high avoided cost rates, creating upward pressure on customer rates. Specifically, EEI argues that it is concerned that states implementing the avoided cost

⁴¹ *Id.* at 9.

⁴² *Id.* at 9-10.

⁴³ *Id.* at 10 (citing 18 C.F.R. §§ 290.102, 292.304 (2010)).

⁴⁴ *Id.* at 10-11 (citing *Southern California Edison Co.*, 70 FERC ¶ 61,215, *reconsideration denied*, 71 FERC ¶ 61,269 (1995) (*SoCal Edison*); *American Paper Institute v. American Electric Power*, 461 U.S. 402 (1983)).

⁴⁵ *Id.* at 12-13 (citing 5 U.S.C. § 553(c)).

provisions of the Clarification Order will result in utilities being locked into long-term contracts at elevated avoided cost rates that create upward pressure on customer rates for years to follow. According to EEI, states are already using tariffs with state-set rates similar to those at issue in this case, and the rates under these programs have sometimes been high. EEI is concerned that state commissions will claim that these high rates meet the avoided cost standard as clarified in the Clarification Order. EEI also argues that, by allowing states greater leeway to set higher avoided cost rates, and to lock those higher rates into long-term contracts, the order departs from the goal of enhanced competition. In addition, EEI argues that, as demonstrated through use of feed-in tariffs in Europe, setting higher rates for particular technologies can lead to high cost consequences and oversupply of those technologies, ultimately leading to a boom-and-bust cycle.⁴⁶

24. Finally, EEI argues that the Clarification Order creates uncertainty, arguing that absent a particular proposal presenting specific facts, and a record that reflects adequate utility and public input, the Commission cannot be sure that the Clarification Order's avoided cost provisions will result in rates that are just and reasonable and no higher than a utility's avoided costs.⁴⁷ EEI contends that, even if utilities face particular energy or capacity percentage or quantity requirements, such as state renewable energy standards, it is unclear why it would be appropriate to set avoided costs for an individual category of QF energy because utilities almost always have a variety of means to meet the requirements. EEI concludes that because utilities are able to satisfy such percentage or quantity requirements without resort to higher avoided costs by QF category, there is no justification for imposing such higher costs. EEI also argues that in light of "the lack of maturity of many QF energy technologies," it is unclear how separate avoided costs for different categories of QF energy or capacity can even be calculated.⁴⁸ According to EEI, allowing avoided cost for a category of QFs to be set based on those QF costs would violate the utility-centric focus of the avoided cost inquiry, and relying upon QF bids in immature sub-markets would effectively allow individual QFs to exercise market power.⁴⁹

25. On December 6, 2010, the Energy Producers and Users Coalition and the Cogeneration Association of California (Energy Producers and Users and Cogeneration Association) filed an answer to the Joint Utilities' request for rehearing of the Clarification Order.

⁴⁶ *Id.* at 13-14.

⁴⁷ *Id.* at 16.

⁴⁸ *Id.* at 15.

⁴⁹ *Id.*

III. Discussion

A. Procedural Matters

26. Rule 713(d) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d) (2010), prohibits an answer to a request for rehearing. We will, therefore, reject the answer submitted by the Energy Producers and Users and Cogeneration Association.

B. Commission Determination

27. For the reasons discussed below, we will deny rehearing of the Clarification Order.

28. We disagree with the arguments of the Joint Utilities and EEI that they did not have adequate notice, and that interested parties did not have the opportunity to provide input on the avoided cost issues raised because the Commission did not act through a rulemaking. The Commission was within its authority to provide guidance in both the July 15 Order and the Clarification Order given that our regulations expressly authorize us to provide guidance in response to petitions for declaratory order to "remove uncertainty."⁵⁰ In response to the two petitions for declaratory order, one filed by the CPUC and one filed by the Joint Utilities, the Commission found in the July 15 Order, that the CPUC's AB 1613 feed-in tariff would *not* be preempted by the FPA, PURPA, or Commission's regulations⁵¹ as long as: (1) the CHP generators from which the CPUC is requiring the Joint Utilities to purchase energy and capacity are QFs pursuant to PURPA; and (2) the rate established by the CPUC does not exceed the avoided cost of the purchasing utility. In the Clarification Order, the Commission merely expanded on the guidance it provided in the July 15 Order, explaining that, should California choose to do so, implementation of a multi-tiered avoided cost rate structure can be consistent with the avoided cost rate requirements set forth in PURPA and the Commission's regulations in that such a cost structure would reflect the costs a utility would avoid.⁵² The guidance

⁵⁰ 18 C.F.R. § 385.207(a)(2) (2010). To the extent that the Joint Utilities and EEI are arguing that the guidance provided in the Clarification Order is not binding because it was provided in response to two petitions for declaratory order, we note that the guidance in the Clarification Order is no less precedential than the guidance the Commission has provided in any other declaratory order.

⁵¹ July 15 Order, 132 FERC ¶ 61,047 at P 65 (citing 18 C.F.R. §§ 292.101 *et seq.* (2010)).

⁵² Clarification Order, 133 FERC ¶ 61,059 at P 22-26.

provided by the Commission in the Clarification Order is a logical extension of the guidance it provided in the July 15 Order. In both orders, the Commission made clear that it was providing guidance on the approaches the CPUC proposed to take, as it was asked to do, and was not ruling on whether the CPUC's actual offer price under its AB 1613 program is, in fact, consistent with the avoided cost rate requirements of PURPA.⁵³ Moreover, the Commission was not required to proceed by rulemaking, but rather had the discretion to proceed by case-specific adjudication – which both the CPUC and the Joint Utilities had requested, and which was within the Commission's discretion.⁵⁴

29. Further, although the Joint Utilities argue that they had no notice that the avoided cost pricing issues would be addressed in this proceeding, the Joint Utilities themselves previously raised arguments in this proceeding pertaining to avoided cost rates. While the Joint Utilities argued in their petition for declaratory order that the issue of what is permitted under PURPA is not relevant in this proceeding,⁵⁵ they nevertheless also asserted that the pricing structure adopted in the CPUC's AB 1613 Decision results in a price above avoided cost.⁵⁶ In their answer to the CPUC's request for clarification of the July 15 Order, the Joint Utilities also acknowledged that the CPUC sought clarification as to how it may determine avoided cost rates for purposes of its AB 1613 program, and responded to the CPUC's arguments regarding what factors the CPUC may consider in determining avoided cost rates.⁵⁷ Because the Joint Utilities themselves have submitted

⁵³ *Id.* P 25 & n.46-47.

⁵⁴ *See, e.g., SEC v. Chenery Corp.*, 332 U.S. 194, 201-203 (1947) (finding that “the choice made between proceeding by general rule or by individual, *ad hoc* litigation is one that lies primarily in the informed discretion of the administrative agency”) (citing *Columbia Broadcasting System v. United States*, 316 U.S. 407, 421 (1942)); *Wisconsin Gas Co. v. FERC*, 770 F.2d 1144, 1166 (D.C. Cir. 1985) (finding that “[i]t is a well-settled principle of administrative law that the decision whether to proceed by rulemaking or adjudication lies within the broad discretion of the agency”).

⁵⁵ Joint Utilities' Petition at 9.

⁵⁶ Joint Utilities' Petition at 7. *See also* Joint Utilities June 3, 2010 Answer, Docket No. EL10-64-000, at 18-19 (arguing that the CPUC cannot substitute its AB 1613 pricing scheme as an alternative method for determining long-term avoided costs for affected CHP facilities, that pricing electricity above avoided cost is not authorized under PURPA, and that the CHP rate set by the CPUC does not reflect avoided costs, as required by PURPA).

⁵⁷ Joint Utilities' August 31, 2010 Answer at 2, 3-13. We also note that the National Association of Regulatory Utility Commissioners filed in this proceeding a

(continued...)

arguments on the avoided cost issue throughout this proceeding, they cannot persuasively claim that they did not have notice that issues pertaining to avoided cost rates may be addressed by the Commission in this proceeding. In addition, the Commission took the unusual step of accepting the Joint Utilities August 31, 2010 answer to the CPUC's request for clarification.⁵⁸ Thus, while the Commission provided additional guidance in the Clarification Order concerning how avoided costs may be calculated, the Joint Utilities had the opportunity to present their arguments, and were therefore afforded due process – and both the Joint Utilities and EEI have filed, and we address here, requests for rehearing.⁵⁹ For these reasons, we reject the arguments on rehearing that interested parties did not have adequate notice.

30. Turning to their substantive arguments, we disagree with the arguments of the Joint Utilities and EEI objecting to the Commission's finding in the Clarification Order that the concept of a multi-tiered avoided cost rate structure can be consistent with the avoided cost rate requirements set forth in PURPA and the Commission's regulations. The Commission's authority under the FPA includes the exclusive jurisdiction to regulate the rates, terms and conditions of *sales for resale* of electric energy in interstate commerce by public utilities.⁶⁰ While section 292.304 of the Commission's regulations sets forth the requirements for *rates for purchases* of electric energy by utilities from

resolution adopted by its membership that expresses its/their support for: “the ability of individual States to determine whether or not the public utilities, under their jurisdiction, should be required to offer to purchase power at prices established by State commissions (including prices set pursuant to State feed-in tariffs) in a manner consistent with federal law”). National Association of Regulatory Utility Commissioners' August 25, 2010 Motion to Intervene Out-of-Time and Answer at Attachment A.

⁵⁸ Clarification Order, 133 FERC ¶ 61,059 at P 18.

⁵⁹ See *Blumenthal v. FERC*, 613 F.3d 1142, 1146 (D.C. Cir. 2010) (finding that, where Connecticut had the opportunity on rehearing to respond to ISO New England's filings and where the Commission considered Connecticut's arguments on rehearing, Connecticut was not denied due process); *State of California ex rel. Lockyer v. FERC*, 329 F.3d 700, 711 (9th Cir. 2003) (Commission provided “all the procedural protections required” when it considered the claims made in requests for rehearing); *accord CNG Transmission Corp. v. FERC*, 40 F.3d 1289, 1293 (D.C. Cir. 1994) (where petitioner had, among other things, opportunity to make its case on rehearing, it had “ample notice and opportunity to be heard”).

⁶⁰ July 15 Order, 132 FERC ¶ 61,047 at P 64 (citing 16 U.S.C. §§ 824, 824d, 824e (2006); e.g., *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988)).

QFs, and while nothing in the regulation requires any electric utility to *pay* more than the “avoided costs for purchases,”⁶¹ it is the *states* that have the authority to dictate a utility’s actual purchase decisions.⁶² Because avoided cost rates are defined in terms of costs that an electric utility avoids by purchasing capacity from a QF,⁶³ and because a *state* may determine what particular capacity is being avoided, the state may rely on the cost of such avoided capacity to determine the avoided cost rate.⁶⁴ Thus, the avoided cost rate may take into account the cost of electric energy from the generators being avoided, *e.g.*, generators with certain characteristics. As explained in the Clarification Order, where a state requires a utility to procure energy from generators with certain characteristics, generators with those characteristics constitute the sources that are relevant to the determination of the utility’s avoided cost for that procurement requirement.⁶⁵ Thus, the

⁶¹ 18 C.F.R. § 292.304(a)(2) (2010); *see, e.g., Connecticut Light & Power Co.*, 70 FERC ¶ 61,012, at 61,023-24, 61,028-030, *reconsideration denied*, 71 FERC ¶ 61,035, at 61,151-53 (1995), *appeal dismissed*, 117 F.3d 1485 (D.C. Cir. 1997) (*Connecticut*).

⁶² *See Pike County Light & Power Co. v. Pennsylvania Public Utility Comm’n*, 465 A.2d 735, 737-38 (1983); *accord e.g., Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354, 371-72 (1988); *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 965-67 (1986); *Kentucky West Virginia Gas Co. v. Pennsylvania Public Utility Comm’n*, 837 F.2d 600, 609 (3d Cir.), *cert. denied*, 488 U.S. 941 (1988); *accord Montana Megawatts I, LLC*, 107 FERC ¶ 61,140, at P 6 (2004) (prudence of power purchases is subject to state commission oversight); *Ameren Energy Marketing Co.*, 96 FERC ¶ 61,306, at 62,189 (2001) (same).

⁶³ 16 U.S.C. § 824a-3(b), (d) (2006); 18 C.F.R. §§ 292.101(b)(6), 292.304 (2010).

⁶⁴ *Small Power Production and Cogeneration Facilities; Regulations Implementing Section 210 of the Public Utility Regulatory Policies Act of 1978*, Order No. 69, FERC Stats. & Regs. ¶ 30,128, at 30,884-85 (1980) (stating that “the value of service from the qualifying facility to the electric utility may be affected by the degree to which the qualifying facility ensures by contract or other legally enforceable obligation that it will continue to provide power” and that “[i]f purchases from qualifying facilities enable a utility to defer or avoid these new planned capacity additions, the rate for such purchases should reflect the avoided costs of these additions”), *order on reh’g*, Order No. 69-A, FERC Stats. & Regs. ¶ 30,160 (1980), *aff’d in part and vacated in part, American Electric Power Service Corp. v. FERC*, 675 F.2d 1226 (D.C. Cir. 1982), *rev’d in part, American Paper Institute, Inc. v. American Electric Power Service Corp.*, 461 U.S. 402 (1983).

⁶⁵ Clarification Order, 133 FERC ¶ 61,059 at P 26; *accord id.* P 22-24.

guidance provided by the Commission in this proceeding simply reflects the reality that states have the authority to dictate the generation resources from which utilities may procure electric energy. Just as, for example, an avoided cost rate may reflect a state requirement that utilities must “scrub” pollutants from coal plant emissions, so an avoided cost rate may also reflect a state requirement that utilities purchase their energy needs from, for example, renewable resources. And while in theory a utility might have a cheaper source of capacity and/or energy available to it, in calculating an avoided cost rate a state may properly look at the actual sources of capacity and/or energy available to the electric utility, rather than at some theoretical source, which is not permitted by state law, that may be cheaper.

31. We disagree with the arguments of the Joint Utilities and EEI that the guidance provided by the Commission is inconsistent with our avoided cost pricing rules and Congress’s intent that utility customers be financially indifferent.⁶⁶ At the outset, we note that, in this proceeding, we have not made any determination as to whether a particular avoided cost rate established by the CPUC meets the requirements of our PURPA regulations. As we have explained, the July 15 Order and the Clarification Order provide a road map for how the CPUC may implement its AB 1613 program consistent with PURPA and the Commission’s regulations. However, we did not have a record to decide, and thus did not decide, whether any particular offer price that the CPUC may ultimately develop using a multi-tiered approach will be consistent with the avoided cost rate requirements of section 210 of PURPA.⁶⁷

⁶⁶ EEI argues that, by allowing states to set different avoided costs for different categories of QFs, the Clarification Order departs from the traditional focus on the cost of alternative energy without regard to energy type. We note that the fact that an interpretation has been “traditional” does not make it inviolate. Previously, states did not mandate particular purchases, e.g., from renewables, and so there was no need to differentiate among generation sources and no need for tiering; all generation sources were essentially fungible, and so our interpretation and the states’ interpretation of our PURPA regulations reflected that fact. That is increasingly not the case; states are now looking to draw distinctions in what they will allow. The orders issued to date in this proceeding, and this order, reflect this change in circumstances.

⁶⁷ Clarification Order, 133 FERC ¶ 61,059 at P 25 & n.46-47 (citing July 15 Order, 132 FERC ¶ 61,047 at P 68). Although we do not decide whether any particular offer price that the CPUC may ultimately develop using a multi-tiered approach will be consistent with our avoided cost rate requirements, with respect to the arguments on rehearing that utility customers must be financially indifferent concerning whether the utility purchases power from a QF or another source, we note that AB 1613 expressly requires that the CPUC set the rates at which the utilities must offer to purchase from

(continued...)

32. EEI also argues that the Clarification Order departs from Congress's intent in PURPA to protect ratepayers from increases in costs. We disagree. PURPA and our regulations nowhere prohibit the concept of a multi-tiered avoided cost rate structure and, indeed, a tiered rate structure to address tiered procurement mandates is consistent with the idea of "avoided cost." Upon review of the statutory language in PURPA, it is clear that Congress did not dictate any particular avoided cost price, but instead stated that rates could not exceed the cost of energy which, but for the QF purchase, a utility would itself generate or purchase. It follows that a state avoided cost rate tied to a state requirement that the utility either build a particular resource or purchase from a particular resource would be no more costly. Pursuant to section 210(a) of PURPA, the Commission prescribed rules imposing on electric utilities the obligation to offer to purchase electric energy from QFs. Section 210(b) of PURPA provides that such purchases must be at rates that are: (1) just and reasonable to electric consumers and in the public interest; (2) not discriminatory against QFs; and (3) not in excess of "the incremental cost to the electric utility of alternative electric energy." Section 210(d) of PURPA, in turn, defines "incremental cost of alternative electric energy" as "the cost to the electric utility of the electric energy which, but for the purchase from [the QF], such utility would generate or purchase from another source."⁶⁸ The Commission implemented this so-called mandatory purchase obligation set forth in PURPA in section 292.303 of its regulations, which provides that "[e]ach electric utility shall purchase, in accordance with § 292.304, ... any energy and capacity which is made available from a qualifying facility...."⁶⁹ Section 292.304, in turn, requires that the rates for such purchases shall: (1) be just and reasonable to the electric consumer of the electric utility and in the public interest; and (2) not discriminate against qualifying cogeneration and small power production facilities.⁷⁰ The regulation further provides that nothing in the regulation requires any electric utility to pay more than the "avoided costs for purchases."⁷¹ "Avoided costs" is defined as "the incremental costs to an electric utility of electric energy or capacity or both which, but for the purchase from the qualifying

CHP generators at a level that "ensure[s] that ratepayers not utilizing [CHP] systems are held indifferent to the existence of [the AB 1613 feed-in] tariff." Cal. Pub. Util. Code § 2841(b)(4) (2010).

⁶⁸ 16 U.S.C. § 824a-3 (2006); *see, e.g., Connecticut*, 70 FERC ¶ 61,012, at 61,023, 61,028.

⁶⁹ 18 C.F.R. § 292.303(a) (2010).

⁷⁰ 18 C.F.R. § 292.304(a)(1) (2010).

⁷¹ 18 C.F.R. § 292.304(a)(2) (2010); *see, e.g., Connecticut*, 70 FERC at 61,023-24, 61,028-030, and 71 FERC at 61,151-53.

facility..., such utility would generate itself or purchase from another source.”⁷² Both section 210 of PURPA and our regulations define avoided costs in terms of costs that the electric utility avoids by virtue of purchasing from the QF.⁷³ The question, then, is what costs the electric utility is avoiding. Under the Commission’s regulations, a state may determine that capacity is being avoided, and so may rely on the cost of such avoided capacity to determine the avoided cost rate.⁷⁴ Further, in determining the avoided cost rate, just as a state may take into account the cost of the next marginal unit of generation, so as well the state may take into account obligations imposed by the state that, for example, utilities purchase energy from particular sources of energy or for a long duration.⁷⁵ Therefore, the CPUC may take into account actual procurement requirements, and resulting costs, imposed on utilities in California.

33. With respect to the Joint Utilities’ argument that *SoCal Edison* is inconsistent with the Commission’s Clarification Order, we find that the Joint Utilities’ argument in this regard misinterprets the guidance provided in the Clarification Order. The Joint Utilities argue that the Commission held in *SoCal Edison* that the CPUC’s process of determining avoided costs did not comply with PURPA because it excluded potential sources of capacity, and that the Clarification Order is inconsistent with this finding. However, the Clarification Order does not permit the CPUC to exclude potential sources of capacity in determining an avoided cost rate. To the contrary, in the Clarification Order the Commission explained that in determining avoided costs the CPUC may take into account actual procurement requirements, and resulting costs, imposed on utilities in California.⁷⁶ The Commission further explained that *SoCal Edison*, in fact, supports the proposition that, where a state requires a utility to procure energy from generators with certain characteristics, generators with those characteristics appropriately constitute the

⁷² 18 C.F.R. § 292.101(b)(6) (2010).

⁷³ 16 U.S.C. § 824a-3(b), (d) (2006); 18 C.F.R. §§ 292.101(b)(6), 292.304 (2010).

⁷⁴ Order No. 69, FERC Stats. & Regs. ¶ 30,128 at 30,884-85.

⁷⁵ See *SoCal Edison*, 70 FERC ¶ 61,215 at 61,676 (acknowledging a state’s ability to favor particular generation technologies is the prerogative of the states, and explaining that “a state may choose to require a utility to construct ... or to purchase power from ... a particular type of resource” and that the state can take such action consistent with PURPA “so long as such action does not result in rates above avoided cost”); *accord id.*, 71 FERC ¶ 61,269 at 62,080 (explaining that a state may, through state action, influence what costs are incurred by the utility in order to encourage renewable generation, and that a state may, in fact, “order utilities to purchase renewable generation”).

⁷⁶ Clarification Order, 133 FERC ¶ 61,059 at P 26.

sources that are relevant to the determination of the utility's avoided cost for that procurement requirement – they are the sources that can sell to the utility, and thus the sources being avoided. It would be illogical to read *SoCal Edison* as authorizing consideration, for purposes of determining a utility's avoided costs, of sources that are, in fact, not able to sell to that utility.⁷⁷

34. We disagree with the Joint Utilities' argument that *Signal Shasta* does not support the guidance provided by the Commission in the Clarification Order. In *Signal Shasta*, PG&E argued that the power purchase agreement filed by Signal Shasta for the sale of power from Signal Shasta's QF to PG&E violated PURPA and the Commission's implementing regulations because Signal Shasta's rates exceeded avoided costs. The Commission disagreed, and *approved* the “‘standard offer’ contract pre-approved by the CPUC,” explaining that “states are allowed a wide degree of latitude in establishing an implementation plan for section 210 of PURPA....”⁷⁸ In doing so, the Commission noted that the power purchase agreement filed by Signal Shasta was an “unmodified Interim Standard Offer No. 4 pre-approved by the [CPUC]” and that it “had a menu of pricing options from which QFs could choose.”⁷⁹ Although the Commission did not address how the CPUC determined energy and capacity prices for the different pricing options, the Joint Utilities' argument that *Signal Shasta* does not support the Commission's finding in the Clarification Order is without merit insofar as the Commission approved the rate schedule containing the CPUC-approved avoided cost rate that was part of “the menu of pricing options from which QFs could choose.”⁸⁰

35. With respect to the various related questions mentioned by the Joint Utilities as necessarily needing answers before states may implement the guidance provided in the Clarification Order, we find that the CPUC should first seek to implement the guidance provided; then, if the Joint Utilities or EEI believe that the CPUC's offer price for its AB 1613 program, as implemented, does not comply with the Commission's avoided cost rate requirements, they have the option of filing a petition pursuant to section 210(h) of PURPA requesting the Commission to enforce its PURPA regulations.⁸¹

⁷⁷ *Id.* P 26-29.

⁷⁸ 41 FERC ¶ 61,120 at 61,295.

⁷⁹ *Id.* at 61,294.

⁸⁰ *Id.*

⁸¹ 16 U.S.C. § 824a-3(h) (2006).

36. Finally, we emphasize that, while the Commission provided guidance on the concept presented by the CPUC, states may have other ways of establishing avoided cost rates that may be consistent with the Commission's PURPA regulations. In this regard, we emphasize that the determinations that a state commission makes to implement the rate provisions of section 210 of PURPA are by their nature fact-specific and include consideration of many factors; our regulations thus provide state commissions with guidelines on factors to be taken into account, "to the extent practicable,"⁸² in determining a utility's avoided cost of acquiring the next unit of generation.⁸³ And those who disagree with a state's implementation may file a petition requesting the Commission to enforce its PURPA regulations.⁸⁴

The Commission orders:

The requests for rehearing are hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

⁸² 18 C.F.R. § 292.304(e) (2010).

⁸³ Clarification Order, 133 FERC ¶ 61,059 at P 24; *accord American REF-FUEL Company of Hempstead*, 47 FERC ¶ 61,161, at 61,533 (1989) (explaining that "states are allowed a wide degree of latitude in establishing an implementation plan for section 210 of PURPA, as long as such plans are consistent with our regulations. Similarly, with regard to review and enforcement of avoided cost determinations under such implementation plans, we have said that our role is generally limited to ensuring that the plans are consistent with section 210 of PURPA..."); *Signal Shasta*, 41 FERC ¶ 61,120 at 61,295; *see also LG&E Westmoreland Hopewell*, 62 FERC ¶ 61,098, at 61,712 (1993).

⁸⁴ *See supra* note 84.