UNITED STATES OF AMERICA 94 FERC ¶ 61,070
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Curt Hébert, Jr., Chairman;
William L. Massey, and Linda Breathitt.

Alliance Companies	Docket Nos. ER99-3144-003, ER99-3144-004 and ER99-3144-005
American Electric Power Service Corporation on behalf of: Appalachian Power Company Columbus Southern Power Company Indiana Michigan Power Company Kentucky Power Company Kingsport Power Company Ohio Power Company Wheeling Power Company	Docket Nos. EC99-80-003, EC99-80-004, and EC99-80-005
The Detroit Edison Company	
First Energy Corporation on behalf of: The Cleveland Electric Illuminating Company Ohio Edison Company Pennsylvania Power Company The Toledo Edison Company	
Virginia Electric and Power Company	
Consumers Energy Company	Docket Nos. ER00-2869-000 and EC00-103-000 (not consolidated)

ORDER ON COMPLIANCE FILING AND PROVIDING FURTHER GUIDANCE, DENYING REQUESTS FOR REHEARING, AND REJECTING FILING ON ALTERNATIVE GOVERNANCE STRUCTURE

(Issued January 24, 2001)

In this order we act on Alliance Companies' [1] compliance filing, direct further

modifications, and deny requests for rehearing. We also provide guidance under the Regional Transmission Organization (RTO) principles [2] which Alliance Companies should incorporate in their compliance filing to this order (compliance filing). In addition, we reject Consumers Energy Company's (Consumers) alternative governance structure filed in Docket Nos. ER00-2869-000 and EC00-103-000.

I. Background

A. Alliance I Order

On December 20, 1999, the Commission conditionally authorized the transfer of ownership and/or functional control of the jurisdictional transmission facilities of several transmission-owning public utilities (Alliance Companies) to the Alliance regional transmission organization (Alliance). [3] The Commission also conditionally accepted under Section 205 of the Federal Power Act (FPA) certain agreements, and conditionally approved the general framework of the filing. We noted that the proposal could provide significant benefits to the industry and consumers if certain aspects of the proposal were modified and/or further developed. [4]

Specifically, with regard to scope and configuration, the Commission stated that because of its geographic location, Alliance would isolate PJM on the east from utilities west of Alliance, this configuration appeared to have strategic implications, and did not meet several factors identified in Order No. 2000. [5] The Commission noted that Alliance would perpetuate the existing situation where Alliance Companies separate buyers and sellers that constitute the predominant west-east trading patterns, and exemplified the concern about strategically located toll gates. Therefore, the Commission stated that Alliance's configuration raised concerns with regard to its proposed scope and configuration. We stated that we would not prescribe how Alliance Companies should resolve these concerns, but noted that it may be possible that Alliance, Midwest Independent System Operator (Midwest ISO), and PJM could negotiate procedures and rate treatments that would eliminate the toll-gate aspect of Alliance's configuration, deal with loop flow issues, and eliminate concerns about reliability impairments.

In addition, we found that Alliance did not meet Order No. 888's [6] and Order No. 2000's independence standard because Alliance Companies' ownership of up to 25 percent of Alliance Publico's stock at formation could allow Alliance Companies effective control of Alliance Publico. We stated that any new utilities could increase the amount of control exercised over Alliance Publico, and Alliance Companies' rights as passive owners in Alliance could allow them to veto the addition of new members or

existing facilities owned by others. We also found that Alliance Companies had not adequately addressed fiduciary responsibilities of the Alliance Board and management to passive owners, and that the proposal would not prevent control, and the appearance of control, of decision-making by any class of participants. Therefore, we directed Alliance Companies to address these concerns in their compliance filing. [7]

We also found that Alliance Companies largely met the tariff administration requirements. However, we reserved judgment on Alliance Companies' non-rate terms and conditions, and most of the issues on rates and transmission pricing pending a compliance filing that addressed full compliance with either the Independent System Operator (ISO) or RTO principles. We further found that Alliance Companies' proposal to continue a form of rate pancaking for up to six years violated the fundamental tenets of the RTO Final Rule, but we noted that we were not closing the door on transition mechanisms that addressed cost shifts. We directed Alliance Companies to revise their proposal so that it required competitive bidding for any contracting of functions, and directed Alliance Companies to amend their filing to provide greater detail and justification regarding the proposed rate, non-rate, and ancillary service provisions.

B. Alliance II Order

In response to the Alliance I Order, on February 17, 2000, Alliance Companies filed a revised proposal. On May 18, 2000, the Commission issued an order on their compliance filing, requests for rehearing, and clarification. We found that with certain modifications, Alliance Companies' proposal to form a non-profit ISO could move forward. However, we also found that the compliance filing submitted by Alliance Companies did not fully satisfy the RTO-related requirements of the Alliance I Order. Therefore, we directed further filings and reiterated elements of the specific guidance previously offered in the Alliance I Order relating to the independence and governance of the Alliance ISO, rate design, scope and configuration, congestion management and redispatch, and coordination with neighboring control areas. [8]

Specifically, we stated that Alliance Companies had not revised their proposal for the active ownership of Alliance Publico. We reiterated that an initial ownership level amounting to a 25 percent ownership block exceeded our 15 percent benchmark, and that Alliance Companies sought to justify their 25 percent ownership level largely on arguments made in their original filing rather than justify their proposal based on guidance provided in Order No. 2000. We also directed Alliance Companies to limit the active ownership to five years or justify a longer period pursuant to Order No. 2000. Furthermore, we directed Alliance Companies to address the independence audit

requirement with respect to Alliance Transco. In addition, we directed Alliance Companies to clarify the fiduciary duty of Alliance Publico, but withheld any final ruling on this issue until the actual corporate documents were submitted to us. [9] We further noted that Alliance Companies were still developing their single-system rate design and resolving their scope and configuration problems. [10]

II. Alliance Companies' September Compliance Filing

On September 15, 2000, as supplemented on September 22, 2000, Alliance Companies filed another compliance filing to comply with the Commission's directives in the Alliance I and II Orders. Alliance Companies state that they plan to create Alliance in the form of Alliance Transco and Alliance Publico, and that Alliance Transco will be formed as a limited liability company that will be controlled and managed by its managing member (an independent entity with no affiliation with a market participant). In addition, Alliance Companies state that Alliance will own and operate transmission facilities that are divested to it by members of Alliance Transco and that Alliance would also operate transmission facilities of non-divesting transmission owners. [11]

Alliance Companies claim that the proposed Alliance, as revised, meets all of the minimum RTO characteristics and functions set forth in Order No. 2000. Alliance Companies further note that they are continuing to develop proposals that will go beyond the minimum characteristics and functions required by Order No. 2000. Alliance Companies state that their Order No. 2000 filing, which they plan to file on or before January 15, 2001, will supplement the proposal in this filing to reflect improvements and address Commission concerns with the proposal. Therefore, Alliance Companies request expedited approval by the Commission by December 15, 2000, so that Alliance Companies can address the Commission's concerns in their RTO filling and begin the process of forming Alliance to commence operations on December 15, 2001. [12]

With respect to scope and configuration, Alliance Companies state that the scope and configuration of the proposed Alliance region is larger than any ISO operating today; that its configuration is appropriate from the electrical topology perspective; and the proposed region is large enough to permit Alliance to maintain reliability, effectively perform its required functions and support efficient and non-discriminatory power markets. [13]

Alliance Companies also claim that their revised proposal satisfies the independence requirement of the Alliance I and II Orders and Order No. 2000. Alliance Companies assert that in the Alliance I and II Orders the Commission directed Alliance

Companies to adopt the requirements of Order No. 2000 for active ownership (voting rights in an RTO). Alliance Companies contend that their revised compliance filing adopts the "safe harbor" and "benchmark" standards and the independence and governance audit requirements in Order No. 2000. [14]

In addition, Alliance Companies assert that the instant filing complies with the Alliance II Order's direction to: (1) clarify that one passive owner of the Alliance may not act singly to exercise approval or veto rights over Alliance's actions to engage in a transaction which the owner deems unrelated to the Alliance's purpose; (2) reformulate the fiduciary duty language to require Alliance and its managing member to disregard uniformly the interests of an Alliance transmission owner in any business asset or liability other than Alliance; and (3) include a conflicts of interest policy consistent with Midwest ISO. Alliance Companies claim that the pro forma Alliance Agreement and the pro forma corporate bylaws comply with these directives and satisfy Order No. 2000. [15]

Alliance Companies also state that they have been involved in discussions with Midwest ISO and some of the transmission owners from Midwest ISO, Southwest Power Pool, and the transmission owners of GridSouth. Alliance Companies state that based in part on these discussions they have prepared a pro forma Inter-RTO Cooperation Agreement (Agreement) to provide a basis for interregional coordination between Alliance and its surrounding regional transmission entities. Alliance Companies explain that this Agreement is intended as an initial draft to provide a framework for Alliance and the neighboring RTOs to build an actual agreement to resolve issues such as congestion management, available transfer capability (ATC) calculations, and security and reliability coordination. Alliance Companies also state that the Agreement contains procedures for rate discounting reciprocity involving three or more RTOs. [16]

With respect to rates, Alliance Companies propose a rate design methodology that they state eliminates multiple transmission access charges (rate pancaking) and permits recovery of quantifiable lost revenues during a transition period in a nondiscriminatory manner. Alliance Companies claim that this proposed rate structure complies with the Alliance I and II Orders to eliminate multiple access charges, minimize cost shifts among customers, remove disincentives to joining an RTO, and establish a level playing field for generators to facilitate a broad regional market. Alliance Companies note that the rates are illustrative only, and that they will submit proposed rates to become effective under Alliance's OATT not later than 60 days prior to the commencement of operations. [17] Thus, Alliance Companies ask that the Commission accept the proposed rate structure and methodology and not the specific rates. [18]

Alliance Companies also note they are currently working internally and in conjunction with other existing or planned regional transmission entities to develop a proposal for using market mechanisms to manage congestion effectively both within Alliance and at its borders with neighboring systems. Alliance Companies state that the revised proposal includes a market monitoring program that will be administered by an independent market monitor, and the market monitor will provide periodic reports to the Commission. Finally, Alliance Companies state that they have submitted an OATT under Section 205 of the FPA, that they assert is consistent with or superior to the Commission's pro forma OATT. [19]

Notices of Alliance Companies' filing, and supplemental filing, were published in the Federal Register, 65 Fed. Reg. 58,065 (2000) and 65 Fed. Reg. 60,416 (2000), respectively, with comments, protests, and interventions due on or before October 6, 2000. On October 4, 2000, the Commission granted requests for an extension of time for filing protests and interventions to and including October 13, 2000. A number of parties filed motions to intervene and protests, and notices of interventions, as listed in Appendix A to this order.

III. Discussion

A. Procedural Matters

The notices of intervention of the state commissions and the timely, unopposed motions to intervene serve to make the intervenors listed in Appendix A parties to this proceeding. See 18 C.F.R. § 385.214 (2000). Given the early stage of this proceeding, and the absence of undue delay or prejudice, we find good cause to grant the untimely, unopposed interventions by certain parties.

Alliance Companies filed answers to various requests for relief and protests. Coalition also filed an answer, requesting that the Commission reject Alliance Companies' answer and transmission rate proposal. Although the Commission's Rules of Practice and Procedures do not generally permit answers to protests and answers to answers (see 18 C.F.R. § 385.213(a)(2) (2000)), given the complex nature of this proceeding and because the answers aided in clarifying certain issues, we will accept Alliance Companies' and Coalition's answers. [20]

On January 8, 2001, Coalition, Coral, Duke Energy North America, L.L.C. (Duke Energy), Enron, Reliant Energy Power Generation, Inc., and Wabash Valley (Indicated Intervenors) filed a motion asking the Commission to appoint a settlement judge to assess the practicalities of a settlement that unites the Midwest Independent System Operator, Inc. (Midwest ISO) and Alliance in a single RTO under Order No. 2000. On January 8,

2001, Cinergy Services, Inc., on behalf of PSI Energy, Inc. and the Cincinnati Gas & Electric Company, and Central Illinois Light Company (Indicated Transmission Owners) filed a motion in support of Indicated Intervenors' motion. On January 18, 2001, Alliance Companies filed an answer opposing the above motions for the appointment of a settlement judge. As discussed below in the scope and configuration section, we are instituting a proceeding before the Chief Administrative Law Judge.

B. Order No. 2000 Guidance

We will address whether Alliance Companies' instant filing is in compliance with the Alliance I and II Orders. In addition, we will provide guidance under the criteria set forth in Order No. 2000, as requested by the Alliance Companies. We note that Alliance Companies filed their Order No. 2000 compliance filing on January 16, 2001, in Docket No RT01-88-000 (January 16 filing). This order does not address the merits of that filing. Rather, we will defer action on the January 16 filing until the parties conclude the technical conferences they intend to hold in March 2001.

Except for the rate aspects of their proposal, Alliance Companies are directed (consistent with their commitment at p. 10 of the January 16 filing) to supplement their January 16 filing to reflect the findings in this order and any agreements reached through the collaborative process, no later than May 15, 2001. Alliance Companies should file their actual tariff rates, terms and conditions no later than 120 days prior to the commencement of operations.

In Order No. 2000 we stated that an RTO must satisfy the following characteristics and functions when it commences operations. [21]

RTO CHARACTERISTICS

RTO Characteristic No. 1: Independence

The RTO must be independent of any market participant.

1. Alliance Companies' Proposal

Alliance Companies propose to create a for-profit transco structure for Alliance. Under their proposed structure, Alliance Companies will create a for-profit transmission entity that would own, control, and operate the jurisdictional facilities of one or more of Alliance Companies and would control -- but not own -- the transmission facilities of the remaining Alliance Companies.

Alliance Companies will establish Alliance by forming two companies, Alliance Transmission Company, Inc. (Alliance Publico) and Alliance Transmission Company, LLC (Alliance Transco). Alliance Transco will be a Delaware limited liability company and will own all the transmission assets divested by the divesting transmission owners. Alliance Transco will control, but not own, the transmission facilities of the remaining Alliance Companies. Alliance Transco will have one managing member and one or more non-managing members. The managing member will be Alliance Publico, a registered public utility holding company that will be owned and controlled by the public through the sale of voting securities in an initial public offering. The managing member will be the sole holder, at formation, of voting Class A securities in Alliance Transco. A transmission owner participating in Alliance will be eligible to own non-voting Class B interests in Alliance Transco if it divests its transmission to Alliance Transco. A non-divesting transmission owner will likewise be eligible to own non-voting Class C interests in Alliance Transco, which interests will be exchangeable for non-voting Class B interests when and if the transmission owner makes a capital contribution to Alliance Transco by the divestiture to Alliance of its transmission. [22]

Alliance Companies state that Alliance Publico will be governed by a board of directors appointed by the shareholders, and that directors of Alliance Publico may not be affiliated with any of Alliance Companies. In addition, they state that no Alliance Company or "Transmission User" under the OATT may purchase more than 5 percent of the stock of Alliance Publico, or hold contract rights otherwise entitling it to direct the voting percentage of such stock. They add that Alliance Transco also will have an advisory committee which will consist of stakeholders from all segments of the industry.

Alliance Companies further state that they have modified certain independence-related features of their proposal as follows. First, Alliance Companies have adopted the Commission's 15 percent benchmark limitation on the ownership of an active interest in an RTO by any class of market participant. Second, Alliance Companies have revised their proposal to provide that no "Market Participant", as defined in Order No. 2000, may retain any voting interest in Alliance Publico after the conclusion of a five-year transition period, absent the express approval of this Commission. Third, Alliance Companies have clarified the rights possessed by a single passive owner of Alliance Transco to approve or veto a business event that the passive owner deems to be extraneous to Alliance's purpose. Lastly, Alliance Companies have formulated a conflicts of interest policy which they claim is consistent with the one adopted by the Midwest ISO.

Alliance Companies note that no modification is needed in establishing the fiduciary duties to divesting and non-divesting transmission owners, asserting that the

Commission has "agreed [with their proposal] . . . with respect to the fiduciary duty owed to passive owners." [23]

2. Intervenors' Comments

Several intervenors [24] assert that Alliance Companies' filing might be interpreted so as to permit any Alliance Company to hold a 5 percent active interest in Alliance while simultaneously holding another 5 percent active interest through an affiliate. In their answer, [25] Alliance Companies dispute this assertion.

Citizen Power states that, according to the Alliance Companies' filing, [26] the Alliance Transco will have no control over rate design until after the close of the transition period, and that the Alliance Companies will instead directly be in control of rate design until the transition period is concluded. Citizen Power claims that this impairs Alliance Publico's independence from Alliance Companies. [27] Enron asserts that Alliance Companies have established a pervasive system of control over Alliance Publico, based on a series of individually small but, when combined, cumulatively significant active and passive ownership (including rights to remove directors, control over the stakeholder advisory process) that results in a corporate structure in which Alliance Publico will not be independent of control or influence by market participants. [28] Enron expresses particular concern that Alliance Companies' proposal could allow Alliance Companies to remove directors essentially at will [29] and Alliance Companies' proposed independence audit, which Enron asserts does not comply with Order No. 2000. [30] Enron also contends that Alliance Publico (which will be part-owned by Alliance Companies) will exercise inappropriate control over the stakeholder input process, by exercising control over the addition of new stakeholder groups, determinations of participant eligibility, and control over drafting voting rules. [31]

Consumer Advocates raise numerous issues with Alliance's proposed corporate control and governance. Consumer Advocates state that Alliance Publico will not be free from control or other influence from market participants, including Alliance Companies.[32] Specifically, Consumer Advocates express concerns regarding: (1) the process of electing directors by Alliance Publico; (2) whether Alliance Companies could combine ownership interests of more than one class to circumvent the Order No. 2000

independence requirements; (3) the retention of certain veto rights (concerning pricing methodology and mergers and asset sales) by transmission owners; (4) the active ownership interests held by Market Participants and the independence obligations of any successor to Alliance Publico or any restructured version of Alliance Publico; (5) the absence of any detailed plans or support with respect to the proposed Alliance governance audit; and (6) the absence of information concerning the structure of the proposed stakeholder advisory committees.

NCEMC asserts that, while Alliance Companies have improved some aspects of their proposal, it is still flawed with respect to independence. [33] NCEMC argues that: (1) the Class B Alliance Transco "put" option (under which Alliance Publico would be required to purchase any Class B interests in Alliance Transco for cash at the then-current "market value" of those interests) is unacceptable; (2) Alliance Companies have failed to limit purchases and sales of goods and services to and from market participants; (3) non-divesting transmission owners of Class C interests in Alliance Transco will retain excessive and unjustified rights; (4) confidentiality requirements applicable to advisory committees are inappropriate; and (5) Alliance Companies have failed to fully satisfy the Commission's independence audit requirement.

Ormet contends that Alliance Companies have failed to adequately describe the role of Alliance Publico in the future. [34] Public Interest Organizations express concern that Alliance will not, in fact, be independent of control by market participants. [35] Public Interest Organizations also argue that: (1) the procedure for providing formal stakeholder input to Alliance has not been adequately developed; (2) the stakeholder process is not public; and (3) there is no requirement that stakeholder positions actually be considered by Alliance Publico or Alliance Transco. [36]

Virginia Commission opposes the inclusion of the Class B "put" right of divesting transmission owners, under which Alliance Publico would be required to purchase any Class B interests in Alliance Transco for cash at the then-current "market value" of those interests. Virginia Commission also asserts that the proposed Alliance independence audit requirements should explicitly require that the selected auditor have no business relationship of any kind with Alliance Transco, Alliance Publico, or any holder of a Class B or Class C interest in Alliance Transco. [37] Virginia Commission expresses concern that stakeholder representatives will be held to excessively stringent confidentiality standards and that their communications with other stakeholders will be inappropriately limited. [38] Virginia Commission is also particularly concerned with the requirement that holders of Class C interests in Alliance Transco must unanimously consent to proposed rate changes during the transition period. Virginia Commission also

states that competing bids should be required when Class B and/or Class C interest holders are seeking to provide goods or services to Alliance. [39] Finally, Virginia Commission reserves its right to review the proposed Alliance corporate structure pending judicial review of Order No. 2000. [40]

3. Discussion

We find that Alliance Companies' filing addresses a number of concerns identified with their prior filings, and, subject to the modifications described in this order, their filing can form the basis for an appropriate RTO filing establishing the independence of Alliance as a for-profit transco.

In the Alliance II Order, we directed "the Alliance Companies to submit corporate documents that conform to" our requirements concerning the fiduciary duties owed to transmission owners. [41] We find that Alliance Companies have complied with this directive.[42]

Under Alliance Companies' proposal, stakeholders are limited in their ability to consult with each other as part of the stakeholder input process and are potentially subject to confidentiality requirements, in that Alliance will control all aspects of membership eligibility, voting, and the formation of new stakeholder groups, and due to the Alliance Companies' proposal to limit stakeholder communications through mandated confidentiality agreements. The processes that stakeholders can use to communicate and consult with an RTO should be developed in consultation with stakeholders. If RTOs are to be responsive to the needs of the market, there must be a meaningful and efficient process for communication and consultation that serves not only the needs of the RTO, but also the needs of stakeholders. We believe that requiring Alliance to unilaterally propose these processes and having the Commission direct changes in processes based on the comments of stakeholders is not the best way to develop workable processes for stakeholder communication and consultation. We believe that a better approach is for the Alliance Companies to develop an advisory process in consultation with stakeholders, and to describe that advisory process and identify the participants. Only if they cannot will the Commission step in.

In their answer, Alliance Companies agree that Alliance Publico should be required to take the "best" bid to provide goods or services, based on objective criteria, whether or not such a bid is submitted by a Class B or Class C interest holder. [43] Alliance Companies indicate that this issue will be addressed further in their executed final agreements which must be submitted as part of their compliance filing, and we will defer further consideration of this issue until that filing.

With respect to active ownership interests, in order to prevent Alliance from expanding the influence of a market participant by creating or issuing any new class of voting security, we note that ownership of any "Other Issuances" as defined in Section 3.3(e) is subject to the ownership restrictions in Order No. 2000 and, to the extent that Alliance intends that ownership of Other Issuances should not be subject to these restrictions, Alliance must submit the terms of Other Issuances for Commission authorization to confirm that its proposed treatment of these Other Issuances is appropriate.

Attachment K defines "Change in Control" to include any transaction resulting in any "person," (as defined in the Securities Exchange Act of 1934) [44] becoming a beneficial owner of more than 50 percent of the voting power of the outstanding voting stock of Alliance Publico. [45] We remind the Alliance Companies that any change in control over Alliance Publico or Alliance Transco requires the Commission's prior authorization under Section 203 of the FPA.

We will reject the Alliance Companies' proposed Attachment K, Section 3.10, which provides transmission owners with veto rights over changes to pricing methodology. In the Alliance II Order, we noted, this is inconsistent with our requirement under Order No. 2000 that the RTO have the exclusive right to set RTO transmission rates. [46] We will also reject the retention by transmission owners of veto rights over mergers and asset transactions, except for matters noted in our prior orders.[47] In the Alliance II Order, we permitted transmission owners to retain a veto right over certain significant business events, such as sale of assets, liquidation, dissolution, winding up or voluntary bankruptcy. We found that the passive owners are entitled to assurance that the business arrangement which they propose, to the extent that we ultimately approve it, will continue as agreed unless they consent to a termination of the business arrangement, and that these types of transactions could cause tax implications of the type that the passive ownership arrangement is designed to prevent. We see no need in this order to expand those veto rights. [48]

Attachment K states that Class A voting units in Alliance Transco shall initially be held only by Alliance Publico as managing member. [49] We note that the ownership of interests in an RTO is subject to the ownership restrictions stated in Order No. 2000, which permit a market participant to hold an active interest in Alliance Publico for up to five years, subject to our limitations on active ownership.[50]

Attachment K also provides for independence audits. [51] In our Alliance II Order, we stated that "the Alliance Companies should address, with respect to their proposed transco, our Order No. 2000 independence audit requirement."[52] Alliance Companies have proposed to chronologically schedule those independence audits consistent with the Commission's requirements but have offered no additional details about the audits themselves beyond that provided in their last filing. Alliance Companies should clarify that the independence audit requirement applies to both Alliance Transco and Alliance Publico.

Attachment L provides that cumulative voting for the selection of directors of Alliance Publico shall not be permitted. [53] We will approve this prohibition, because cumulative voting could otherwise be a means for circumventing the independence requirements of Order No. 2000. Attachment L also provides for the appointment of advisory directors, who will serve only during periods of special appointment. [54] If advisory directors may vote, this voting right might circumvent our limitations on who may govern the RTO. We direct Alliance Companies to specify that no advisory director may be granted voting power and to modify Attachment L, Article III, Section 10 accordingly.

With respect to the "put" right for Class B interests, Alliance Companies note that their proposed procedure for the valuation of these interests has not yet been developed.[55] We clarify that we do not, in this order, reach this rate making issue. Any departure from traditional rate practices must satisfy the requirements in Section 35.34(e) of our regulations[56] and will be evaluated when and if proposed in a specific rate case.

RTO Characteristic No. 2: Scope and Regional Configuration

The RTO must serve an appropriate region.

1. Alliance Companies' Proposal

Alliance Companies' continue to propose a transmission service area which extends from portions of Michigan into portions of Indiana, Ohio, Kentucky, Pennsylvania, Tennessee, West Virginia, Virginia, and North Carolina, comprising nine states and including 40,000 miles of transmission lines. [57] In this respect, their application is unchanged from their two prior filings. However, they now provide additional information concerning scope, including certain affidavits and supporting information [58] concerning trading patterns in and near Alliance Companies' proposed

RTO service area, and other data concerning pricing behavior and electrical topography. Alliance Companies state that this configuration comports with the Commission's regional configuration factors. [59]

2. Intervenors' Comments

Numerous intervenors protest Alliance Companies' proposed scope and configuration. Many of the intervenors argue that: (1) the proposed scope and configuration are inappropriate; (2) the scope and configuration have not changed since Alliance Companies' last proposal; (3) the reciprocity discount provisions of the Inter-RTO Agreement do not mitigate the flawed scope; (4) with such scope and configuration, Alliance will simply act as a toll gate; and (5) the proposal will perpetuate historical trading patterns and fails to take market competition and efficiency into account. [60]

Additionally, various intervenors raise specific areas of concern regarding scope and configuration. For example, Buckeye asks that the Commission direct all Ohio utilities to join either Midwest ISO or Alliance. [61] Enron argues that the proposed scope will not successfully internalize parallel path flows due to the Alliance area's interdependent relationships with PJM, the New York Power Pool, and SERC. [62] Midwest ISO notes that the prevailing pattern of transactions using Alliance Companies' systems are west-to-east power flows and, accordingly, Alliance Companies form an essential part of the market. Midwest ISO also requests that the Commission limit its analysis on scope and configuration to the facts presented in Alliance Companies' prior filings and instant compliance filing, and not consider the recent announcements by various Midwest ISO participants that they intend to join Alliance. [63] PSE&G asks that the Commission direct Alliance Companies to revise their filing so that the proposed RTO can be fully integrated with PJM, New York, New England, and Ontario markets. [64] State Commissions claim that Alliance Companies' proposal fails to: (1) address the extent to which Alliance's operations will be adversely affected by the absence of additional members, particularly those located at Alliance's regional borders; (2) identify the procedures and rate structures Alliance will implement when coordinating its operations with adjacent utilities; and (3) explain why it is not feasible for them to join with other groups forming RTOs to expand their RTO service area. [65] State Commissions also claim that Alliance Companies' proposal fails to establish a clear regional structure, and fails to resolve Lake Erie loop flow issues. [66] Finally, Wabash Valley requests that only a single RTO be approved in the Midwest region. [67]

3. Discussion

In our previous orders, the Commission identified the concerns it had with Alliance Companies' proposed scope and configuration, but reserved judgment on the issue pending further filings by the Alliance Companies.[68] Much has changed since those orders issued. For example, Alliance Companies have proposed a new rate design which incorporates a single rate for through and out transactions which eliminates the pancaking that was present in Alliance Companies' prior proposal. This new rate design mitigates, to a significant extent, our concerns regarding the "toll gate" aspect of Alliance Companies' proposed scope and configuration. Moreover, in their RTO filings submitted in October of 2000, Dayton Power and Light Company (Dayton) and Northern Indiana Public Service Company (NIPSCO), indicated that they will join Alliance.[69] The addition of Dayton and NIPSCO, located to the west of the Alliance Companies, will increase the scope and configuration of Alliance and should allow Alliance to more effectively internalize parallel flows. We note also that Alliance Companies will incorporate regional power flows in their calculation of ATC and commit to develop and implement procedures to address parallel flows with other regions within three years as required by Order No. 2000.[70] Finally, we note that in Order No. 2000,[71] the Commission found that an RTO could potentially meet the scope and configuration requirements through a contract that eliminates the effect of seams separating RTOs. Alliance Companies indicate that they are engaged in an inter-RTO seams collaborative with Midwest ISO, Southwest Power Pool (SPP) and the transmission owners of GridSouth, SPP and the Midwest ISO, and that tentative resolution has been reached on inter-RTO planning and the facilitation of one-stop shopping.[72] This agreement will have a mitigating effect on our previously expressed concerns regarding Alliance's configuration which spans two NERC regions.

While the above-referenced developments are sufficient to allow us to reach a finding that Alliance's scope and configuration are consistent with the requirements of Order No. 2000, we also note that Illinois Power Company has signed the Alliance Agreement and may ultimately become a member of Alliance.[73] In addition, the Commission, in an order issued concurrently with this order, is providing Midwest ISO and Alliance Companies with the opportunity for further discussions to resolve their differences. Regardless of the outcome of those negotiations, it is clear that Alliance is expanding. Therefore, in consideration of the foregoing, we find that Alliance Companies' proposed scope and configuration are consistent with Order No. 2000.

RTO Characteristic No. 3: Operational Authority

The RTO must have operational authority for all transmission facilities under its control.

1. Alliance Companies' Proposal

Operating Protocol

Alliance Companies state that their Operating Protocol sets forth the framework and process that will be used to operate the transmission system for Alliance. Alliance Companies state that under the Operating Protocol, Alliance will have functional control of the transmission systems of Alliance Companies. According to Alliance Companies, Alliance will: (1) implement and administer the OATT and OASIS; (2) act as NERC Security Coordinator; (3) promote the development of an ancillary services market; (4) coordinate the scheduling of all transmission system maintenance and generator maintenance; (5) monitor transmission use behavior; (6) determine and facilitate the relief of congestion; (7) calculate ATC; (8) interface with future power exchanges that may be established in the Alliance region; and (9) implement performance/audit criteria by which it will judge the operation and performance of the transmission owners with respect to functions shared with or delegated by Alliance to the transmission owners. [74]

In addition, Alliance Companies state that the Operating Protocol sets forth some of the responsibilities of the Transmission Owners and Users, including that the Transmission Owners will physically operate their transmission systems at the direction of Alliance. Transmission Owners also will continue to operate their respective control areas consistent with the directions of Alliance as the NERC Security Coordinator. In addition, the Transmission Owners will provide Alliance with all the necessary data to support the ATC calculations.

Alliance Companies also state that Alliance will have the ability to direct temporary functional control over non-transferred transmission facilities in order to prevent or remedy a system emergency. However, if Alliance determines that it needs additional transmission under its control (or less facilities), it is limited to recommending that the Transmission Owners transfer the facilities to Alliance. [75] Furthermore, Alliance will develop, in consultation with the Transmission Owners, operating procedures governing its functional control of the transmission facilities.

2. Intervenors' Comments

NCEMC states that the proposed RTO will have inadequate authority to determine which transmission facilities it needs to control. [76] Specifically, NCEMC argues that if

Alliance determines that additional facilities should be under its functional control, it can only recommend, and not order the transfer. [77] AMP-Ohio argues that "One Stop Shopping" is hampered since control over individual Delivery Points still rests with the Transmission Owners that have not divested or over which control has not been transferred. [78]

3. Discussion

We find that Alliance Companies have satisfied RTO Characteristic 3 and find that Alliance has, at a minimum, functional control over all transmission facilities transferred to it in this application. In any event, if any party believes that it has been subject to undue discrimination, it may file a complaint with the Commission under Section 206 of the FPA. We previously observed in the Alliance I Order that Alliance Companies' proposed Operating Protocol provides that Alliance can exercise temporary functional control over non-transferred facilities in order to prevent or remedy system emergencies. [79] We continue to believe that this provision is sufficient in the first instance to ensure the reliability of Alliance. We note that the details of a process to determine whether or how to implement the transfer of additional facilities should be part of the larger discussion of transfer of facilities from the transmission owner to Alliance, as discussed below in our disposition of the requests for rehearing of the Alliance II Order. Finally, AMP-Ohio's concerns regarding control over delivery points should be addressed by Alliance Companies in the context of the operating procedures governing functional control of the transmission facilities which they commit to develop.

RTO Characteristic No. 4: Short-Term Reliability

The RTO must have exclusive authority for maintaining the short-term reliability of the grid that it operates.

1. Alliance Companies' Proposal

Alliance Companies indicate that Alliance will have exclusive authority for maintaining the short-term reliability of the grid that it operates since it will be the exclusive authority for receiving, confirming and implementing all interchange schedules, including implementation of interchange schedules for control areas not operated by Alliance. [80] Additionally, Alliance will implement any necessary Transmission Loading Relief (TLR) events. Alliance Companies add that such authority

will be implemented directly or through Transmission Owners operating at Alliance's direction. [81] Alliance will also have the authority to direct redispatch of generating units for reliability purposes as well as the authority to approve or disapprove scheduled outages of transmission facilities owned by others. [82] Alliance Companies state that Alliance will operate under the reliability standards established by NERC and will report to the Commission if such standards hinder it from providing reliable service. [83]

2. Intervenors' Comments

Enron argues that Alliance Companies' proposal retains existing control areas within Alliance and may lead to Alliance favoring generation that Alliance Companies own or control to the disadvantage of control area operators or their affiliates. [84] Enron requests that control over reserving and scheduling transmission should rest with Alliance. [85] Ormet requests that we mandate a date certain for the consolidation of control areas within Alliance. [86]

3. Discussion

We are generally satisfied that Alliance Companies have met our requirements for maintaining short-term reliability of the grid. Enron's protest is without merit. The Operating Protocol state unequivocally that Alliance will schedule all transactions under the OATT. [87] Furthermore, while we will not mandate a date certain for the consolidation of control areas within Alliance as Ormet requests, we note and remind Alliance Companies of their commitment to evaluate the consolidation of control areas within 18 months of commencement of service and to report such findings to the Commission. [88]

RTO Function No. 1: Tariff Administration and Design

The RTO must administer its own transmission tariff and employ a transmission pricing system that will promote efficient use and expansion of transmission and generation facilities.

1. Alliance Companies' Proposal

Alliance Companies' proposed transmission rates are discussed in this section. Other terms and conditions of the OATT will be discussed in Section IV of this order.

Pricing Protocol

In response to our direction in the Alliance I and II Orders to eliminate rate pancaking and to address concerns regarding the effect of the pricing proposal on Michigan Customers, [89] Alliance Companies propose a transitional rate structure that includes non-pancaked zonal rates applicable to deliveries to loads within Alliance and a single regional rate applicable to deliveries to load outside Alliance. Alliance Companies maintain that the transitional pricing structure is intended to eliminate pancaking, ensure non-discriminatory pricing, minimize cost shifting, and ensure revenue neutrality for transmission owners during the transition period. Alliance Companies state that: (1) they are seeking approval only of the proposed methodology; (2) the rates contained in the filing are for illustrative purposes; and (3) the actual rates will be filed at least sixty days prior to the commencement of Alliance's operations.

In addition, Alliance Companies propose a moratorium on the transitional pricing structure that would remain in effect through December 31, 2004, unless the transmission owners unanimously agree to an earlier termination date. The proposed Pricing Protocol provides for two exceptions to the rate moratorium on zonal rates during the transition period; i.e., a transmission owner may file for an adder to its zonal rate to recover the cost of new investment incurred by a transmission owner when that cost exceeds 150 percent of the transmission owner's cumulative depreciation expense incurred since the transmission service date; and the moratorium shall not apply unless innovative rate treatment (other than a rate moratorium) is accepted by the Commission.

Prior to the end of the transition period, Alliance Companies intend to commence a process for developing a post-transition pricing structure which will provide economically efficient incentives for use and expansion of the transmission system and siting of new generation and propose to have such pricing in place so that it can go into effect no later than January 1, 2005. Alliance Companies state that the proposal submitted by Alliance will be designed to ensure that a provider of last resort subject to a state rate moratorium does not incur trapped costs, including stranded costs. [90]

Zonal Rates for Drive In and Within Transactions

Alliance Companies state that the transitional pricing structure is based upon license plate zonal rates for transmission customers delivering to loads located within a particular Alliance zone (i.e., intrazonal, drive-in, or within transactions), with no

multiple access charges. The zonal rates have two components: a zonal facilities charge (ZFC) plus a zonal transition adjustment (ZTA). [91] The ZFC will be either: (1) the applicable transmission owner's effective transmission rate established under its individual OATT; or (2) if the transmission owner so elects, a rate developed in accordance with the innovative rate proposals described in Order No. 2000. [92] The ZTA is designed in conjunction with the region-wide rate discussed below to recover a revenue shortfall during the transition period. Alliance Companies state that the ZTA reflects the historical transmission charges that the Alliance transmission owner in a particular zone has paid to other Alliance transmission owners to serve load within its own zone. Alliance Companies state that the ZTA is designed to collect additional revenue from each zone in proportion to the benefits that the particular Alliance Company will realize when it no longer has to pay pancaked rates for transmission purchased from another Alliance company to serve load within its zone. Under the proposal, the stated rate for each zone will apply to both network and point-to-point transactions. Initially, there will be five zones, with each zone encompassing the transmission facilities of one of the Alliance Companies. [93] Alliance Companies state that as new transmission owners join Alliance during the transition period, new zonal rates will be established in the same way. Alliance Companies maintain that for every transaction that involves generation and load in different zones, the proposal would substantially reduce transmission costs to the customer.

Region-Wide Rate for Through and Out Transactions

Alliance Companies propose a single region-wide rate for all transactions that serve loads outside Alliance. Alliance Companies refer to this rate as the Region-Wide Rate for Through and Out Transactions (RTOR). Alliance Companies state that the RTOR is designed to recover the remainder of the revenues lost (due to the elimination of pancaking) that are not already collected under the ZTA. The numerator of the RTOR rate will be calculated by determining the total revenues associated with through and out transactions that would be lost due to the elimination of rate pancaking, and deducting from that figure (i) the revenues recovered through the ZTA and (ii) credits for short-term firm and non-firm through and out service. The denominator will equate to the long-term firm billing determinants that remain after the formation of Alliance. Alliance Companies state that the region-wide rate will likely represent an increase in charges under current rates to transmit power from an Alliance zone to a location outside of Alliance that is directly interconnected to that zone. However, out transactions which involve multiple zones will realize a rate reduction as the pancaked charges are replaced by a single region-wide rate.

2. Intervenors' Comments

Intervenors complain that Alliance Companies' proposal, particularly the ZTA, perpetuates rate pancaking. [94] Intervenors complain that Alliance Companies' proposal actually contains two rates for load inside Alliance, the ZFC and the ZTA, and that the combination of these two components yields a pancaked rate yet again. Citizen Power states that Alliance Companies' two-part pricing system proposal fails to address the problems that the Commission identified in Alliance Companies' original two-part proposal which consisted of a zonal rate plus a regional access charge. [95]

Intervenors argue that in proposing a rate moratorium, Alliance Companies have not complied with Order No. 2000's filing requirements. [96] Citizen Power asks that the Commission direct Alliance Companies to revise its rate moratorium to comply with the filing procedures mandated by Order No. 2000. [97] Virginia Commission states that the proposed moratorium is a type of performance based RTO rate incentive that the Commission said it would consider in Order No. 2000. However, Virginia Commission argues that the filing is deficient because Alliance Companies have failed to include a cost-benefit analysis as required by Order No. 2000.

Some intervenors complain that zonal rates are discriminatory because similarly situated customers can end up paying two different rates. [98] Intervenors state that the ZTA is designed to spread the lost revenues only across the customers located within the zone that imports the power and thus the effect is discriminatory because similarly situated customers in different zones will pay two transmission rates, depending on which area is being controlled by the RTO. [99] There is also concern among intervenors that similarly situated customers located within Alliance, but not in the same zone, will be paying different rates.

Intervenors complain that the pricing structure is flawed, [100] that the proposal outlined by Alliance Companies lacks specifics and support [101] and that many concepts need further explanation and clarification. [102] For example, Buckeye complains that the proposal includes no quantitative cost support and requests that the Commission reserve

judgement on the conceptual proposal until such time as the Alliance Companies file cost of service revenues and calculations of claimed lost revenues.

AMP-Ohio claims that Alliance should use the pro forma method for calculating the network rate (i.e., the load ratio share), and not the stated rate proposed by the Alliance Companies.

Additionally, Wolverine complains that because it is surrounded by, and dependent upon Consumers for transmission, under Alliance Companies' proposal it can only recover revenues through Alliance for the use of its transmission system if it can reach an agreement with Consumers. According to Wolverine, this could put it in a difficult position because Consumers may view Wolverine's participation in Alliance as a potential loss of revenue to Consumers.

3. Discussion

In the Alliance I Order, the Commission directed Alliance Companies to eliminate pancaked rates, but this directive was without prejudice to Alliance Companies proposing a different transition mechanism that addresses quantifiable revenue lost and cost shifts. [103] In the Alliance II Order, the Commission stated that it would not take any further action with respect to the pancaking issue until Alliance Companies filed their new rate proposal. However, the Commission reiterated that Alliance Companies' ultimate proposal should also address our concerns about the effect of their original proposal on Michigan customers. [104]

In this filing, Alliance Companies propose to eliminate rate pancaking by using a license plate rate for deliveries within Alliance and a system-wide rate for transactions which go out of or through Alliance. With respect to the transmission rate for deliveries within Alliance, the zonal rate design, we find that Alliance Companies' proposed zonal rate that includes a component for lost revenues (ZTA) is a reasonable approach to eliminate rate pancaking for transactions within Alliance. The proposed ZTA is a relatively small component of the rate that attempts to recover revenues from each zone equal to the benefit that each zone receives from the elimination of rate pancaking and thus links the costs and benefits associated with the elimination of rate pancaking. Moreover, the proposed license plate approach adequately addresses the concerns expressed in the Alliance II Order regarding Michigan customers as it preserves the benefits accruing to those customers under the Consumers/Detroit Edison (ITC) joint tariff. However, for the reasons discussed below, we are requiring revisions to the proposed methodology for determining the RTOR.

As discussed above, the RTOR is designed to collect the remainder of the revenues lost due to the elimination of pancaking that would otherwise result in cost shifts but which are not collected through the ZTA. The resulting rate, $2.10 kW/mo., is provided for illustrative purposes; however, Alliance Companies state that they expect that the final rate will not differ significantly.[105] The Commission finds that the method used by Alliance Companies to address lost revenues and cost shifts is reasonable but the resulting rate is unacceptable because it produces an excessive rate differential between the price of transmission service to loads located within Alliance versus the price of transmission service to loads located outside Alliance. [106] While we believe it is appropriate to provide flexibility for RTO participants to propose rate structures that minimize rate disincentives associated with RTO formation, the differential between the RTOR rate and rates for delivery within Alliance is simply too large to be reasonable.

However, while we do not accept this aspect of Alliance Companies' proposal, we would consider a RTOR that is designed consistent with the rate design used to develop the zonal rate. We note that a RTOR based on the highest zonal rate in the region would recover approximately 70 percent of the identified lost revenue, and the increased throughput that would result from the adoption of a single (lower) rate may provide for the recovery of some, perhaps all, of the remainder. If not, we would then be open to a methodology that would collect, through the ZTA, the remaining lost revenue not recovered as a result of increased throughput. Moreover, we note that in an order issued today in Illinois Power, Docket No. EL01-123-000, the Commission provided for negotiations between Alliance Companies and Midwest ISO. We believe that the potential for Commission approval of a RTOR even higher than the highest zonal rate in Alliance is greater given the increased benefits that a larger Midwest RTO would likely produce.

With respect to Alliance Companies' proposed post-transition rate proposal, we note that the proposal contains a "Hold Harmless for State Frozen Rates" provision. [107] This provision requires Alliance to design the post-transition pricing structure to ensure that a provider of last resort subject to a state rate moratorium does not incur trapped costs. The proposal states that Alliance may meet this requirement in a number of ways, one of which involves Alliance indemnifying and holding the provider of last resort harmless from such losses. This approach, if adopted by Alliance, would appear to make Alliance the guarantor of recovery of trapped costs. This aspect of the proposal appears problematic. However, because it may be unnecessary for Alliance to indemnify a transmission owner from trapped costs, we will defer consideration of this issue until Alliance seeks recovery of such costs.

We turn now to intervenors' arguments as they relate to other (non-RTOR) aspects of Alliance's proposal.

As noted above, intervenors argue that the rate proposal is discriminatory because similarly situated customers that reside in different zones pay different rates. We disagree. The Commission has previously approved the use of license plate rates in the ISO context (e.g., PJM[108]) and in Order No. 2000, reiterated that the license plate approach is a reasonable transition mechanism. [109]

Alliance Companies also propose a rate moratorium on changes to the zonal and regional rates for transmission service, and, as noted above, intervenors are opposed to it. In response to intervenor arguments that the proposed moratorium is inconsistent with the requirements of Order No. 2000 because it is not supported with a cost-benefit analysis, Alliance Companies maintain that the instant filing is a compliance filing, and there is no requirement in the Alliance Orders for a cost-benefit analysis. After consideration, we will defer ruling on the rate moratorium until Alliance Companies complete their filing.

In response to intervenors' arguments that the proposal lacks specifics and requires additional support, we find that the proposal contains enough information to allow us to accept the methodology proposed for the zonal rate aspect of the application, but we agree that additional support is necessary before approval of specific rates will be granted. Therefore, when Alliance Companies file for approval of actual rates, that filing should include a detailed explanation of the rate proposal (including all assumptions relied upon), as well as workpapers and supporting documentation that will allow verification of the calculations used in the development of the rates contained in the filing.

Alliance Companies propose to use a stated rate methodology to calculate network rates. Intervenors believe that the load ratio share method better captures and allocates the effects of growth in transmission usage. Consistent with our finding in PJM, we find that the stated rate for network service is reasonable as it provides greater rate certainty to suppliers and customers. [110] For purposes of open access transmission service, either approach is acceptable.

In response to Wolverine's argument that it can only recover revenues through Alliance for the use of its transmission system if it can reach an agreement with Consumers, we reiterate our statement in Order No. 2000-A that all transmission owners should be compensated for the use of their facilities, although we cannot conclude in this order what types of compensation methods should be used in a particular circumstance.

[111] Consistent with Order No. 2000-A, [112] we direct Alliance Companies to develop a method to compensate all transmission owners for the use of their facilities, including the facilities of Wolverine. We encourage Alliance Companies to work with Wolverine and other transmission owners to develop a method to ensure that all transmission owners are treated fairly. We encourage the parties to use the Commission's Dispute Resolution Service or settlement judge procedures.

Coalition complains that the zonal facilities charge (ZFC) may provide for the recovery of revenue losses due to the elimination of pancaked rates. In support, Coalition cites Pricing Protocol 2.1.1(c) which includes the following sentence: "Unless the affected Transmission Owner agrees, it [the ZFC] shall not provide for recovery of any revenue losses due to the elimination of 'pancaked' rates." Coalition states that the implication of this sentence is that the ZFC can reflect revenue losses arising from the elimination of pancaking if a transmission owner were to agree. The basis for this sentence is unclear, therefore, we direct Alliance Companies to clarify this sentence in their compliance filing to this order.

RTO Function No. 2: Congestion Management

The RTO must ensure the development and operation of market mechanisms to manage transmission congestion. The RTO must satisfy the market mechanism requirement no later than one year after it commences initial operation. However, it must have in place at the time of initial operation an effective protocol for managing congestion.

1. Alliance Companies' Proposal

Alliance Companies state that they are currently working internally and in conjunction with other existing or planned regional transmission entities to develop a proposal to use market mechanisms to manage congestion effectively both within Alliance and at its borders with neighboring systems. Alliance Companies state that they intend to include the proposal, or an alternative market-oriented proposal in their Order No. 2000 filing. They also assert that in the event that a market-based approach to congestion management is not in place on the first day of operations, Alliance will have effective procedures in place for managing congestion on that date and will have a market-based congestion management program in place within one year of commencement of operations.

Alliance Companies further state that to maintain transmission service, Alliance may redispatch generation or curtail load, or reschedule generation and/or approved transmission maintenance. To implement congestion management solutions, Alliance

Companies, as a part of their interconnection agreements with generators, will require generators to provide redispatch bids for congestion management. Alliance Companies assert that under the OATT, Attachment K, Transmission System Congestion Management, parties that provide congestion management services will be compensated by Alliance at the applicable bid prices (not to exceed such party's authorized charges if subject to regulatory approval). In addition, for start-up generators or rescheduling planned generation or transmission maintenance, Alliance will compensate the affected parties at a price negotiated between the parties.

Alliance Companies explain that the costs associated with managing congestion will be separated into two components, zonal and regional. The zonal rate will reflect the actual congestion management costs incurred in the respective zone. However, Schedule 11 of the OATT identifies the historical cost of congestion within the zone and serves as an estimate of the cost of congestion for that zone. The regional component captures congestion costs above what has historically occurred (i.e., due to regional tariff operations), and will be recovered uniformly from all transmission customers under the OATT.

Alliance Companies also state that they will provide information regarding options that transmission customers may pursue to protect non-firm transactions from curtailment and to facilitate the provision of a new request for transmission service that would otherwise be rejected due to congestion. In this regard, Alliance will publicly identify potential generation redispatch options that, if enacted, would have a significant mitigating impact on the congestion. In addition, Alliance Companies state that Alliance will also seek bids for reassignment of transmission.

2. Intervenors' Comments

Intervenors complain that Alliance Companies' congestion management proposal lacks detail, and that more specific information is needed. Allegheny Energy asserts that the proposed hybrid scheme of congestion management based in part on Locational Marginal Pricing (LMP) and in part upon flow-gate tracking and market redispatch concepts has not yet been successfully demonstrated. [113] Consumer Advocates request that Alliance Companies clarify the statement that impacts of redispatch will be reflected in imbalance statements. [114]

PSE&G argues that although the filing notes that a market-based congestion management system will be proposed a year from now, the instant filing fails to address market-based congestion management. PSE&G states that the filing alludes to "competitive locational pricing" but does not propose to implement LMP or recognize

that efficient congestion prices are derived from a RTO-coordinated bid-based dispatch and related balancing market priced at the marginal cost of redispatch. PSE&G also argues that the filing fails to contain any concrete proposals for defining and allocating financial transmission rights. [115]

Alliance Companies respond that intervenors raise congestion management issues that are beyond the scope of this proceeding. Additionally, Alliance Companies argue that in the Alliance I and II Orders, the Commission found that Alliance Companies' proposed congestion management proposals are consistent with the Midwest ISO's proposals. However, the Commission also required all generators located on the Alliance system to bid to provide redispatch service. [116] Alliance Companies indicate that because the instant submittal includes such a requirement, and because they intend to include a long-term congestion management plan in their RTO compliance filing, these issues are beyond the scope of this proceeding.

3. Discussion

We find that Alliance Companies have complied with our direction in the Alliance II Order that all generators connected to Alliance's system bid to provide redispatch service.

We find that intervenors' concerns that Alliance Companies' instant proposal lacks a detailed market plan for congestion management are premature. Under Order No. 2000[117] market mechanisms to manage transmission congestion need only be in place within one year of commencement of service. We note that Alliance Companies commit to have such a program in place. In the interim, we find that Alliance Companies' congestion management plan represents an effective protocol for managing congestion. However, we encourage Alliance Companies to consider the comments of intervenors, especially those of PSE&G, Allegheny Energy, and PJM in designing its final market mechanism congestion plan proposal. [118]

RTO Function No. 3: Parallel Path Flow

The RTO must develop and implement procedures to address parallel path flow issues within its region and with other regions. The RTO must satisfy this requirement with respect to coordination with other regions no later than three years after it commences initial operation.

1. Alliance Companies' Proposal

Alliance Companies state that Alliance will internalize parallel path flows within the Alliance region, and where parallel flows can be identified Alliance will include them in its ATC calculations. Alliance Companies assert that within three years after it commences operation Alliance will develop and implement procedures to address parallel flows with other regions, and have included in their filing the pro forma Inter-RTO Cooperation Agreement which would require participating RTO's to address parallel flows on an interregional basis.

2. Intervenors' Comments

Enron argues that Alliance Companies' current scope and configuration will not internalize parallel path flows because of the region's interdependent relationships. [119]

3. Discussion

We find that Alliance Companies' proposal to address parallel path flows is consistent with our requirements in Order No. 2000. First, under Section 3.1.4 of the Operating Protocol, Alliance will include regional parallel path flows in its ATC calculation. Second, contrary to Enron's assertion, Alliance's scope is expanding and such expansion enables increased internalization of parallel path flows in the region. Moreover, under Section 3.1.4 of the Operating Protocol, and Sections 3.10 and 4.5 of the Planning Protocols, Alliance Companies commit to implement procedures to address parallel path flow issues between regions. Finally, Section 6 of the pro forma Inter-RTO Cooperation Agreement requires signatories to have procedures in place to address parallel path flow issues no later than December 15, 2004. [120]

RTO Function No. 4: Ancillary Services

The RTO must serve as a provider of last resort of all ancillary services required by Order No. 888 and subsequent orders.

Alliance Companies state that Alliance will provide ancillary services under the OATT and will serve as the ancillary services provider of last resort. However, to the extent permitted by the OATT, transmission customers will have the option of acquiring their own ancillary services. Alliance Companies also state that Alliance will have the authority to decide the minimum required amounts of each ancillary service and, if necessary, the locations at which these services must be provided. Alliance Companies explain that the OATT provides a separate rate schedule for each ancillary service, and

within each rate schedule a separate charge for each pricing zone. Ancillary services will be provided separately for each control area. [121] Alliance Companies assert that initially, the charges for all ancillary services, except Energy Imbalance Service, will represent a pass-through of the costs charged by the relevant control area operator or third party.

With respect to Energy Imbalance Service (Schedule 4), Alliance Companies propose to provide this service upon the commencement of operations through a real-time balancing market that is operated either by Alliance or by an independent market operator. Alliance Companies state that the charge for this service will be based on the imbalance market price for each pricing zone and that there will be no true-up mechanism, such as a bandwidth with time-shifted energy payback.

4. Intervenors' Comments

Intervenors' protests focus on the proposed energy imbalance services and energy imbalance market. Intervenors address the appropriateness of such market, potential abuses in the market, the lack of detail with respect to the operation of the market, the function of the market monitor with regard to the market, and the use of pricing on a zonal basis. [122] Other intervenors claim that the scope of the proposal is too narrow (i.e., should include a secondary market where entities could trade and offset imbalances). [123] Intervenors also request numerous changes be made to the imbalance proposal (e.g., lengthen the settlement window, and eliminate imbalances that are not the fault of the customer). [124] Finally, intervenors argue that the charges for Regulation and Frequency Response Service (including the penalty for unauthorized usage) are excessive and discriminatory. [125]

In their answer, Alliance Companies state that energy imbalance prices will be determined for each pricing zone based on the energy bid into the imbalance market and utilized by that market. [126] Alliance Companies explain that imbalance pricing within a pricing zone will be a function of generators bidding into the market, their location, total quantities of generation bid into the market, and losses. According to Alliance Companies, transmission customers should be subject to imbalance pricing in their pricing zone for action taken in that zone.

Alliance Companies also state that settlement for imbalances will be based on the difference between actual and scheduled energy. Energy imbalances will be charged to parties taking energy from the system, such as over-consuming load and under-producing generation. Parties supplying energy to the system, such as under-consuming load and over-producing generation, will be paid an imbalance price. Alliance Companies assert that a secondary market, in which entities may trade and offset their imbalances, is not

presently necessary to permit the day-one start-up of Alliance Companies' imbalance market.

5. Discussion

Alliance Companies' proposal to serve as the provider of last resort for all ancillary services and to provide transmission customers with access to a real-time balancing market is consistent with the requirements of Order No. 2000. In addition, we agree with Alliance Companies that a secondary imbalance market is not required at the initial operation date. However, we find that Alliance Companies' proposal lacks sufficient details. Intervenors have raised a number of concerns regarding the operation of the proposed energy imbalance market, and we direct Alliance Companies to address these concerns when they make their compliance filing to this order. For example, Alliance Companies should address concerns regarding the adequacy of competition in the market. Alliance Companies should also explain the relationship of the market monitor in connection with ancillary services markets, and in particular, the energy imbalance market. [127] Alliance Companies must also provide detailed support explaining the operation of the real-time balancing market including support for the proposed settlement window of between 5 and 15 minutes.

In addition, we reject intervenors' arguments that the zonal ancillary rates are discriminatory. The current configuration of Alliance is based on separate control areas (zones) with separate license plate rates in each zone, and the proposed ancillary service prices (based on zonal rates rather that system-wide rates) are consistent with that approach. However, one of the benefits of operating a transmission system regionally is that some ancillary services can be provided by regional resources rather than local resources. We expect Alliance Companies will look for and take advantage of opportunities to make them available to consumers. We also reject the argument that the penalty for unauthorized usage of Schedule 3, Regulation and Frequency Response Service, is unreasonable. We find that the proposed penalty is intended to discourage unauthorized use of the service and is consistent with our policy of allowing penalties equal to twice the stated rate.

RTO Function No. 5: OASIS and Total Transmission Capability (TTC) and ATC

The RTO must be the single OASIS site administrator for all transmission facilities under its control and independently calculate TTC and ATC.

1. Alliance Companies' Proposal

Alliance Companies state that Alliance will operate a single OASIS site to receive and process all transmission service requests, and that Alliance will independently calculate TTC and ATC. Alliance Companies explain that Alliance will calculate ATC values on a control area basis and will determine values from one hour to one year into the future, consistent with Commission requirements, and that ATC calculations will identify and adjust for parallel path flows within Alliance and on neighboring systems. In addition, Alliance Companies assert that Alliance will coordinate ATC calculations with neighboring systems by sharing base data, identifying mutual impacts and providing data in support of the NERC Interregional Security Network, and that such coordination should result in consistent TTC/ATC values across interfaces.

2. Intervenors' Comments

Public Interest Organizations assert that while the OATT states that Alliance will be responsible for the final ATC calculation, the OATT also states that transmission customers will provide source and sink information to the transmission provider and all control area operators responsible for ATC calculations. Therefore, they contend that it is unclear whether Alliance, the transmission provider, or the individual control area operators are responsible for the final ATC calculation. [128]

3. Discussion

Under Alliance Companies' Operating Protocol, Alliance will operate a single OASIS site to receive and process all transmission service requests and Alliance will independently calculate TTC and ATC. [129] Therefore, we find that Alliance Companies' proposal complies with RTO Function No. 5. While Public Interest Organizations correctly note that transmission customers will provide certain information to both Alliance and control area operators, the protocols are clear that Alliance will be making the calculation and Alliance will create a system for tests and checks to ensure customers of coordinated and unbiased data. Accordingly, no further clarification is necessary. Alliance Companies are directed to file the system of tests and checks to be used by Alliance when Alliance Companies make their compliance filing.

RTO Function No. 6: Market Monitoring

To ensure that the RTO provides reliable, efficient and not unduly discriminatory transmission service, the RTO must provide for objective monitoring of markets it operates or administers to identify market design flaws, market power abuses and opportunities for efficiency improvements, and propose appropriate actions.

1. Alliance Companies' Proposal

Alliance Companies state that Alliance's market monitoring program will be implemented by an independent market monitor who will monitor markets operated, and services provided, by Alliance. Alliance Companies explain that the market monitor will provide periodic reports to the Commission and respond to requests from the Commission or other interested parties for additional data and analysis. Alliance Companies also state that the market monitoring program will identify anticompetitive actions related to the operation of transmission or generation facilities that result in transactions or operations that are unduly discriminatory or preferential, or that provide the opportunity for the exercise of market power. [130]

2. Intervenors' Comments

Intervenors state that Alliance Companies' proposal lacks specificity and fails to provide sufficient explanation and details regarding how the proposed independent market monitor will fulfill its role and how the monitoring plan will operate. [131] Intervenors argue that Alliance Companies have not provided sufficient assurance that there will be an effective entity to perform market monitoring and enforcement functions to protect consumers from the exercise of market power. [132] Chaparral states that Alliance Companies' proposed market monitoring program will not adequately ensure non-discriminatory transmission service and will permit abuses in Alliance's ancillary services market. Chapparral contends that market monitoring is not effective because it occurs after the fact, and that the Commission itself must monitor the potential for market abuses. [133]

3. Alliance Companies' Answer

Alliance Companies assert that their market monitoring program is consistent with, and in some respects exceeds the requirements of Order No. 2000, and that intervenors have not identified any aspects of the proposal that are inconsistent with Order No. 2000. Alliance Companies note that they have proposed an independent market monitor even though Order No. 2000 does not require it. [134]

In response to the State Commissions, Alliance Companies admit that some of State Commissions' suggestions are reasonable and appropriate. Specifically, Alliance Companies commit that the market monitor: (1) will have no affiliation with market participants; (2) will be operational on the date Alliance provides transmission service, and (3) should have the authority and resources to obtain documents and information

necessary to carry out its mandate. Alliance Companies also maintain that because Alliance will not operate or administer a commodity market, it would be inappropriate for Alliance to monitor commodity markets except to detect behavior that might affect the efficiency of markets that Alliance will operate. [135] Alliance Companies request that the Commission address these issues when Alliance Companies file the OATT as a rate schedule 60 days prior to the commencement of operations as an RTO. [136]

4. Discussion

In Order No. 2000, the Commission determined that market monitoring is an important tool for ensuring that markets within the region covered by RTOs do not result in transactions or operations that are unduly discriminatory or preferential or provide the opportunity for the exercise of market power. [137] The Commission stated that the market monitoring plan should indicate whether the RTO will only identify problems or whether it will also propose solutions. The Commission also stated that the market monitoring plan should clearly identify any proposed sanctions or penalties and the specific conduct to which they would be applied, provide the rationale to support any sanctions, penalties, or remedies (financial or otherwise) and explain how they would be implemented. [138]

After considering Alliance Companies' market monitoring proposal, we agree with intervenors that Alliance Companies' plan lacks sufficient details. While Alliance Companies have outlined the broad structure of the market monitoring program and the market monitor's duties, the proposal fails to explain how the program will actually function and how the market monitor will perform its duties.

Therefore, we direct Alliance Companies to resubmit their market monitoring plan with further details on the program and the scope of the market monitor's authority. We also encourage Alliance Companies to meet with interested parties to craft a plan which satisfies the Commission's goals as expressed in Order No. 2000, and meets the needs of both Alliance, and those who will use its services. In this regard, we note that Alliance Companies have already accepted several of the State Commissions' suggestions.

In Order No. 2000, the Commission did not prescribe a particular market monitoring plan, or the specific elements of such a plan, because market monitoring is evolving as trading markets are created. The Commission provided for a flexible approach and noted that different market monitoring plans may be appropriate for different RTOs. [139] In addition, the Commission stated that it would periodically assess the need for, and degree of, market monitoring that should be done. [140] In this proceeding, we direct Alliance Companies to resubmit their market monitoring plan and

also give notice that the Commission may issue a supplemental order regarding market monitoring. Based on the experience we gain from observing the various market monitoring plans proposed in the RTO filings, and based upon our review of how well the various plans meet our goals, we may issue a supplemental order to revise and/or further define, among other things, the roles and responsibilities of the market monitor, the data to be provided to or collected by the market monitor, the interaction of the market monitor with the Commission's staff, as well as other aspects of market monitoring.

RTO Function No. 7: Planning and Expansion

The RTO must be responsible for planning, and for directing or arranging, necessary transmission expansions, additions, and upgrades that will enable it to provide efficient, reliable and non-discriminatory transmission service and coordinate such efforts with the appropriate state authorities. If the RTO is unable to satisfy this requirement when it commences operations, it must file with the Commission a plan with specified milestones that will ensure that it meets this requirement no later than three years after initial operation.

1. Alliance Companies' Proposal

Alliance Companies state that Alliance will be responsible for planning the transmission system, and it will adopt a planning process that will be open and transparent. Alliance will hold final responsibility for the regional transmission plan, subject to approval by regulatory and other entities with approval authority. Alliance Companies assert that Alliance's planning and system expansion process will enable it to provide efficient, reliable and non-discriminatory transmission service, and will encourage market-driven operating and investment actions for preventing and relieving congestion. They also state that Alliance will accommodate efforts by state regulatory commissions to create multi-state agreements to review and approve new transmission facilities.

In addition, Alliance Companies' Planning Protocol [141] imposes on Alliance the responsibility for developing and annually updating a regional transmission plan. [142] As part of the planning process, the Planning Protocol provides for the establishment of three panels - a Planning Advisory Committee (PAC), a Reliability Planning Committee (RPC), and an Operational Planning Committee (OPC). [143] The PAC is intended to ensure that all market participants have input into the planning process. The RPC is intended to facilitate joint planning between Alliance, transmission owners, and local distribution utilities. The OPC has the responsibility to monitor planning compliance with the

operational planning criteria and to provide a forum for interested parties to resolve disputes.

2. Intervenors' Comments

Public Interest Organizations assert that the Planning Protocol must be modified because it does not explicitly require RTO consideration of all grid enhancement options for meeting reliability needs and addressing congestion problems. Public Interest Organizations add that the Planning Protocol does not require that RTO selection of a preferred system expansion alternative be based on long-term, least-cost system planning principles. [144]

3. Discussion

The Commission finds that as modified below, Alliance Companies' proposed Planning Protocol meets the requirements of Order No. 2000. Specifically, we find that Alliance Companies' Planning Protocol does not state how or by whom the members of the PAC, RPC, and OPC will be appointed, what their terms or constituencies will be, nor does the Planning Protocol set forth the grounds for removing them, if any. We believe that this information is important to establish the vitality and openness of the planning process. Therefore, we direct Alliance Companies to revise the Planning Protocol to include this information when they make their compliance filing.

In addition, we agree with Public Interest Organizations that Alliance should consider all grid enhancement options for meeting reliability needs and addressing congestion problems, and our review indicates that the protocol provides for such consideration. For example, the PAC (as described and properly constituted), will provide a forum for stakeholders and interested parties (like Public Interest Organizations) to provide input into the planning process, and the PAC, in turn, will provide input to Alliance in the development of the regional plan. Similarly, while the protocol does not specifically mention that grid enhancements will be based on long-term least cost principles, the protocol requires that the most efficient project be undertaken. [145]

RTO Function No. 8: Interregional Coordination

The RTO must ensure the integration of reliability practices within an interconnection and market interface practices among regions.

1. Alliance Companies' Proposal

Alliance Companies state that their pro forma Inter-RTO Agreement (Agreement) (Attachment P) was developed to provide a basis for interregional coordination between Alliance and its surrounding regional transmission entities. Alliance Companies assert that it provides a basis for sharing information, developing common practices, and coordinating operations among the RTOs participating in the Agreement. However, Alliance Companies also state that the Agreement is an initial draft that provides a working framework for reaching agreement on how to resolve seams issues. Thus, Alliance Companies request that resolution of specific issues be deferred until the agreement is filed under Section 205 of the FPA.

2. Intervenors' Comments

APPA & NRECA recommend that the Commission reject the Agreement. PJM states that it is eager to pursue inter-regional discussions with Alliance Companies and others, and asks that the Commission direct Alliance Companies to discuss inter-regional proposals with PJM and other grid operators. Thus, PJM also asks that the Commission defer action in this proceeding on the Agreement until an executed agreement is filed with the Commission under Section 205 of the FPA, with the full support of neighboring RTOs. Allegheny Energy asks that the Commission endorse the cooperation concept but allow the details to be negotiated by the parties. Alliance Companies respond that they are ready to discuss seams issues and other approaches to inter-RTO relations with PJM.[146]

3. Discussion

In Order No. 2000, the Commission stated that:

> We expect the RTO to work closely with other regions to address inter-regional problems and problems at the 'seams' between RTOs. . . An RTO proposal must explain how the RTO will ensure the integration of reliability and market interface practices. . . Coordination of activities among regions is a significant element in maintaining a reliable bulk transmission system and for the development of competitive markets. Order No. 2000 at 31,167-168.

Although Alliance Companies have filed a pro forma Agreement to provide a basis for interregional coordination, the Agreement was not filed as a final executed agreement. Rather, Alliance Companies filed the Agreement as an initial draft that was intended as a working framework for Alliance and neighboring RTOs to reach agreement on how to resolve seams issues.

While we are not acting on the Agreement at this time, we reiterate the importance of the Midwestern entities reaching an agreement on seams issues. The Commission believes that the development of a properly functioning regional energy market requires an arrangement that provides a seamless market over a large geographic area. Consistent with this belief, the Commission, in an order issued today in Illinois Power Company, Docket No. ER01-123-000, directs the Chief Administrative Law Judge to facilitate discussions among the Midwestern entities.

We also note that neighboring utilities, Allegheny Energy and PJM, both urge the Commission to endorse the concept of inter-regional cooperation and request that the Commission direct that they negotiate further instead of ruling on this initial draft agreement. Accordingly, we also direct Alliance Companies to continue discussions with Allegheny Energy, PJM, and other entities within the region to further develop resolutions to seams issues. Therefore, we will not act on Alliance Companies' Agreement at this time.

IV. Open Architecture

Any proposal to participate in an RTO must not contain any provision that would limit the capability of the RTO to evolve in ways that would improve its efficiency, consistent with the required characteristics and required functions for an RTO.

Alliance Companies claim that their proposal is based upon open architecture that permits adjustment to accommodate changes in the electric industry through fluid provisions in the proposed protocols, pro forma agreements, and the transitional rate mechanism. No party has filed comments on this aspect of the proposal. We believe that Alliance Companies' proposal is consistent with our requirements for open architecture. However, we will reserve final judgment until Alliance Companies make their compliance filing.

V. Specific OATT Issues

A. Rate Issues

Administrative Fee

1. Alliance Companies' Proposal

Alliance Companies propose to charge an administrative fee on all transactions, including transactions by transmission owners for transmission service for bundled load and grandfathered contracts. The administrative fee will be collected under Schedule 10 of the OATT through formula rates consisting of two charges: a Transaction-based Charge (TBC) billed on a per transaction basis, and a Capacity-based Charge (CBC) billed on a MW per hour of reserved capacity or network load basis, as applicable.[147] Alliance Companies have identified categories of costs to be recovered through these charges (e.g., labor, start-up costs, operating expenses, taxes), but not a specific level of costs. Alliance Companies have divided costs into four service categories that may be recovered under either the TBC or CBC as follows: (1) manage transmission and ancillary service reservations, (2) manage energy schedules, (3) manage transmission and ancillary services, and (4) common costs.

2. Intervenors' Comments

Intervenors [148] complain that the formula is vague and should not be approved until more detail is filed. Intervenors are concerned that the administrative fee may be exorbitant as applied to small transmission users since it is assessed on a schedule basis and does not consider the size or duration of transactions. Intervenors state that many of the costs to be recovered through the TBC do not vary with the number of transactions (e.g., costs incurred to provide and maintain the capability to accept or deny reservations do not increase with the number of transactions processed). Intervenors also argue that the administrative fee should not be collected since presumably each transmission owner already has included costs into its rates for administration of its individual OATT. Finally, intervenors contend that the administrative fee, in addition to all of the other charges, leads to rate pancaking. Therefore, intervenors request that the administrative fee be rejected or set for hearing.

3. Alliance Companies' Answer

Alliance Companies respond that as with other rate aspects, they only seek approval of the methodology for calculating the administrative fee and not a specific level for the charge, which will be filed prior to the effective date of Alliance. Alliance Companies also state that the administrative fee, along with the zonal rates, will not

recover duplicative costs because the fee is designed only to recover Alliance's costs, and the methodology specifically excludes recovery of costs to be recovered from the zonal rates under Schedule 10.

4. Discussion

We find that Alliance Companies have not shown that their method for recovery of administrative costs is just and reasonable. In particular, we are concerned with the use of transactions as a means to allocate costs, and the lack of a transparent fee for services provided by Alliance. However, rather than rejecting the proposed administrative fee methodology or setting it for hearing as various intervenors request, we direct Alliance Companies to address intervenors' concerns and support their methodology with detailed cost support that will allow verification of their results when they file their actual rates in compliance with this order.

Loss Methodology

1. Alliance Companies' Proposal

Alliance Companies propose that transmission customers self-supply or arrange for the supply of energy to compensate for real power losses, and propose an initial methodology for the determination of those losses. Under this initial methodology Alliance Companies state that the amount of energy the transmission customer must provide to compensate for real power losses will be based on the Alliance pricing zone entry points and delivery points, expected power flow distribution over the Alliance zones, and the seasonal on peak/off peak/shoulder peak loss factors to be included in a loss matrix in Attachment M to the OATT and posted on OASIS. Alliance Companies also propose each reservation be sufficient to include the amount of energy plus losses rounded up to the next MW. Alliance Companies state that the pricing zone loss factors will be updated every two years and filed with the Commission no later than 3 months prior to their effective date. Alliance Companies also assert that this methodology will be evaluated every two years, and thereafter Alliance will notify the Commission whether it will continue the methodology or replace it with one that more accurately identifies the marginal impact of transactions on losses.

2. Intervenors' Comments

Coalition argues that this methodology is inappropriate because: (1) it rounds losses to the next whole MW which may be burdensome for small schedules and may have a cumulative adverse affect on ATC; and (2) it cumulatively applies each zone's loss

factor for multi-zone deliveries which fails to take into account the physics of transmitting from zone-to-zone (e.g., moving from lower-voltage facilities to higher-voltage facilities). Coalition also claims that the e-Tag schedule should clarify that losses are included in the total schedule to avoid potential imbalance problems. Buckeye contends that the loss calculation does not recognize that "Holidays" occur during weekdays, and thus should be classified as off-peak periods for losses. [149] NCEMC argues that the proposed calculation factor for losses includes a cumbersome pancaking of losses. [150] Finally, Wabash Valley maintains that Alliance Companies' loss methodology, in addition to all of the other charges, leads to rate pancaking. [151]

Alliance Companies respond that their loss methodology does not violate the Commission's policy against pancaking since the pancaking policy applies to transmission access charges which have been eliminated. Furthermore, Alliance Companies state that while losses will vary for different transactions, such variance appropriately characterizes the nature of losses and, therefore, their proposal attempts to approximate the actual losses incurred.

3. Discussion

We find that Alliance Companies' loss methodology is unclear and requires further explanation. Specifically, Alliance Companies have not demonstrated why it is necessary to round schedules up to the next whole MW. Coalition raises valid concerns as to the effect of this requirement on small transmission users and ATC calculations that must be addressed by Alliance Companies. In addition, Alliance Companies have not demonstrated that its cumulative approach to determining losses for multi-zone transactions is reasonable. Finally, we agree with Buckeye's argument regarding holidays and direct Alliance Companies to account for holidays in their compliance filing to this order. Therefore, Alliance Companies are directed to respond to intervenors' arguments and to further explain and justify their proposal in their compliance filing to this order. Intervenors will have an opportunity to challenge the methodology and specific factors when those actual loss factors are filed with the Commission.

Grandfathered Agreements

1. Alliance Companies' Proposal

Alliance Companies state that a transmission owner providing transmission service under a grandfathered contract shall take transmission service as a transmission customer under the terms of the OATT commencing on the transmission service date.

Alliance Companies' Pricing Protocol provides that the transmission owner will be charged only the ZTA for service to grandfathered contracts under Schedules 7, 8 and 9 of the OATT and will not be charged for ancillary services under OATT Schedules 2, 3, 5, and 6, or for losses under OATT Attachment M to the extent they can self-provide these services. Alliance Companies' Pricing Protocol also provides procedures for the renegotiation of grandfathered contracts. In addition, Section 38 of the OATT provides that following the transition period, all transmission customers, including those taking service for bundled load and grandfathered contracts, shall be subject to the pricing terms and conditions of the OATT. Finally, in compliance with the Alliance I and II Orders, Alliance Companies have submitted a list of grandfathered contracts.

2. Intervenors' Comments

Coalition argues that under Alliance Companies' proposal, transmission services under grandfathered contracts are subject to mandatory conversion to the OATT at the end of the transition period which may contravene the provisions in long-term transmission agreements. Coalition also contends that Alliance Companies do not definitively address the Commission's requirement that rate pancaking under grandfathered contracts must be eliminated. Buckeye asserts that Alliance Companies have incorrectly stated that the Power Delivery Agreement (PDA), referenced as a grandfathered contract in the OATT, expires on December 31, 2002. Buckeye claims that this agreement continues through June 2003, and asks that this error be corrected.

AMP-Ohio also notes that following the transition period, customers served under grandfathered contracts will be converted to the OATT and argues that the Commission should not allow Alliance Companies to abrogate these contracts without a public interest showing. State Commissions argue that many of the grandfathering concepts included in the Pricing Protocol need further explanation.

Alliance Companies respond that two corrections are needed in the list of Grandfathered Contracts. First, the service agreement between Detroit Edison and DECo Merchant Operations should not be listed as a grandfathered agreement and second, Buckeye is correct that its PDA terminates in June 2003.

3. Discussion

In Order No. 2000, the Commission stated that it would address the issue of existing transmission contracts on an RTO-by-RTO basis, rather than resolve the issue generically. We encouraged each RTO to address how and when it might convert existing contracts, and to submit a contract transition plan which contains specific details

about the procedures to be used involving the conversion from existing contracts to RTO service. [152]

Alliance Companies' proposal regarding grandfathered contracts properly contains procedures for renegotiation of such agreements, with the ultimate goal being that all customers begin taking service under the OATT at the end of the transition period. However, under Alliance Companies' proposal, customers served under grandfathered contracts that are unable to renegotiate their contracts will be automatically converted to service under the OATT at the end of the transition period. We find that it is premature to accept this aspect of the proposal at this time.

However, while it is premature to accept Alliance Companies' proposal at this time, we find that an RTO can operate an efficient, reliable transmission system only to the extent that all transactions are governed by consistent terms and conditions. Often, grandfathered agreements include terms and conditions that interfere with optimal regional operations, and the customers' desire to maintain grandfathered agreements is often driven by economic considerations. Therefore, we direct the parties to all grandfathered contracts (not just renegotiable contracts[153]) whose terms extend beyond the transition period to negotiate amendments or termination of such contracts, and, in particular, to find ways to address economic considerations that do not perpetuate conflicting terms and conditions of service in the long term. To aid the parties in their renegotiation efforts, the Commission will direct the Director of the Commission's Dispute Resolution Service [154] to convene a meeting of the parties to assist them in determining if it is possible to arrange a process that may foster negotiation and agreement between them. If by December 31, 2003, renegotiation of any of these contracts has not been achieved, we direct Alliance to notify the Commission regarding these contracts. In this filing, Alliance should: (1) identify these contract(s); (2) clarify the unresolved issues; and (3) propose a remedy.

Failure to Curtail Penalty

1. Alliance Companies' Proposal

Alliance Companies seek to impose on transmission customers a $50 per kW penalty for failure to curtail pursuant to the transmission provider’s directive. [155] Alliance Companies state that this charge shall apply only to the portion of the service that the transmission customer fails to curtail in response to a curtailment directive.

2. Intervenors' Comments

Intervenors argue that the penalty for failure to curtail is unreasonable since it exceeds the maximum penalty under Commission's policy, i.e., twice the stated rate. They also claim that the penalty is not justified, and that the tariff fails to adequately specify the response time and the requested actions that must be taken by customers during load shedding and curtailment events.

3. Discussion

Alliance Companies claim that the penalty is justified because a customer's failure to comply with a curtailment directive could result in a serious system failure. Moreover, Alliance Companies argue that since Alliance will not own generation, it is critical that sufficient sanctions exist under the tariff to ensure curtailment orders will be followed.

While we agree that a penalty may be appropriate, we find that the proposed penalty exceeds that needed to encourage compliance with curtailment directives. Alliance Companies must either delete the penalty or propose a new penalty that is consistent with our precedent on penalties. Moreover, if Alliance Companies choose to include a new penalty provision, they must explicitly delineate the response times and actions required of customers at the time of curtailment prior to imposing a penalty for failure to curtail. [156]

B. Non-Rate Issues

1. Point-to-Point Transmission Service

Alliance Companies propose to modify Section 13.7, Classification of Firm Transmission Service, to provide that reservations not exceeding three years may be made pursuant to an umbrella firm point-to-point service agreement if requested on the OASIS. Section 13.7 is also modified to specify a penalty for a customer's usage in excess of its reservation. [157]

Coalition argues that the proposal permits aggregation in that all generators located within a Pricing Zone be treated as a single receipt point and loads located within a Pricing Zone be treated as a single delivery point. [158] Coalition also objects to the penalty provision.

We find that the proposal is consistent with the pro forma tariff and is accepted. Coalition is incorrect that Section 13.7 provides for aggregation of generators or loads.

The section merely provides (as does the pro forma tariff) that multiple generating units at the same plant can be treated as a single receipt point. [159] Similarly, the proposed penalty provision is consistent with those previously accepted by the Commission. [160]

2. Modifications On a Non-Firm Basis

Under the pro forma tariff, a transmission customer taking firm point-to-point service may receive transmission service on a non-firm basis over secondary receipt and delivery points in amounts not to exceed its firm reservation without incurring an additional non-firm point-to-point transmission charge. Alliance Companies propose to extend this provision to non-firm service without requiring a new request for service on OASIS. [161] Alliance Companies state that the total charge for this new service will not exceed the comparable charge for firm point-to-point transmission service. Alliance Companies have also modified Section 22.1(c) to clarify that a transmission customer retains its original firm or non-firm right to schedule service.

Coalition states that allowing non-firm customers to "flex" to alternate points is a worthwhile innovation in principle, but is susceptible to discriminatory application. Coalition argues that this provision should be accepted only if the tariff is modified to require that: (1) requests to substitute alternate points will be made on OASIS thereby making them transparent and open to monitoring, (2) the option should be made available on a non-discriminatory basis, and (3) the conditions of service should be filed at the Commission rather than simply posted on OASIS. [162]

We find that the proposed service provides additional flexibility to transmission customers, and we accept it subject to Alliance Companies requiring that requests for such service be made on OASIS. With this requirement, we believe that application of the service will be transparent and available on a non-discriminatory basis.

3. Network Transmission Service

Several intervenors have concerns regarding Article III of the OATT, Network Integration Service. Buckeye argues that under Section 32.2, the customer should have an additional 30 days to review System Impact Study (SIS) results. [163] Coalition complains that: (1) under Section 30.2, Alliance Companies have inappropriately assigned short-term network resources the same reservation priority as short-term firm point-to-point requests, and (2) off-system sales from designated network resources should not be permitted without first un-designating those resources as this would give generation owning utilities an advantage over power purchasing utilities. [164]

With respect to Buckeye's argument, Alliance Companies' proposal under Section 32.2 is consistent with the pro forma tariff and we see no reason to provide additional time to review the SIS. We do, however, agree with Coalition and reject as inconsistent with our precedent Alliance Companies' proposal in Section 30.2 to accord a request for a designation of network resource of less than one year the same reservation priority as short-term firm point-to-point service. [165] Accordingly, Alliance Companies are directed to delete this language from Section 30.2 of the Alliance OATT. Finally, we also agree with Coalition that firm off-system sales from designated network resources should not be permitted without first un-designating those resources. As we indicated in Order No. 888-A, reliability of service to network and native load customers could be affected absent a requirement that network resources always be available to meet a customer's network loads. [166] Thus, Alliance Companies are directed to delete the reference to firm sales under Section 30.4 of the Alliance OATT.

4. Scheduling

The Alliance OATT, Section 14.6, provides that all requests for non-firm point-to-point service (except requests for hourly service) made during the first 15 minutes after the time when non-firm point-to-point service can first be requested will be considered as if they were submitted at the same time.

In response, Coalition states that queue position only matters if there is insufficient ATC to accommodate all requests, and in that situation, it is not clear which of the requests deemed to be submitted simultaneously would be honored. Coalition contends that the best solution would be to give simultaneous requests reservation priority rankings based on the same factors used to assign curtailment priorities. In any event, Coalition maintains that whatever approach is taken, more specificity is required.

We find that Alliance Companies' proposed tariff modification is reasonable as it is consistent with previously accepted proposals. [167] In response to Coalition, Section 14.2, Reservation Priority, which follows the pro forma tariff, is clear that in the event of a system constraint, competing requests of equal duration will be prioritized based on the highest price offered by the customer for such service.

5. Rollover Rights

Section 2.2 of the Alliance OATT maintains the pro forma tariff's reservation priority for existing firm service as well as the requirement that a customer exercising

rollover rights match any longer term request. Rollover rights are also extended to retail customers and are limited to the facilities which were included, or could be included, within the costs of the pricing zone where the firm service customer had taken service.

Coalition argues that under Section 2.2, rollover rights should apply to all of Alliance's facilities rather than only those associated with the zone in which the customer is located. [168]

Alliance Companies' proposed language in Section 2.2 is similar to language proposed by Midwest ISO and accepted by the Commission. [169] As we stated in Midwest ISO, limiting a customer's rollover privileges to the facilities that are included in a customer's present rates implements the requirements of the pro forma tariff in the context of a regional arrangement. Every customer under the Alliance OATT will have the same rollover rights it enjoys today under individual tariffs – no more, no less. Creation of rollover rights associated with capacity that is not used presently to serve the transmission customer would result in rollover rights that far exceed the existing capacity used today to provide transmission service to existing customers.

6. Sequential Off-Peak Hourly Service

Alliance Companies propose a new service, Sequential Off-Peak Hourly Service, as part of Alliance's Non-Firm Point-To-Point Transmission Service. [170] According to Alliance Companies, this service enables efficient use of the transmission system because customers will have more flexibility in scheduling off-peak, hourly, non-firm service because customers can reserve this service over daily, weekly, or monthly periods, whereas under the pro forma tariff, requests for hourly non-firm service may not be submitted prior to noon the day before the service. Alliance Companies propose under Section 18.3 of the OATT that customers reserving Sequential Off-Peak Hourly Service do not have the right to match requests for longer-term non-firm services that may displace them under the bumping provisions of the tariff.

Coalition contends that the parameters of the proposed service are unclear and that the proposal should be supported with more detail before it can be considered or accepted. Among other things, it questions where transactions under this service would fit in the OATT's priority queues. [171]

Alliance Companies' proposed Sequential Off-Peak Hourly Service is very similar to the service we accepted in FirstEnergy Operating Companies, 88 FERC ¶ 61,010

(1999) (FirstEnergy). In FirstEnergy, we stated that such a service was consistent with the pro forma tariff, as long as the bumping provisions were not upset, because it simplified the reservation process for off-peak, hourly, non-firm services without changing any of the priorities set forth in the pro forma tariff. [172] While Alliance Companies' proposal contains the clarification on priorities under Section 18.3, we direct Alliance Companies to include the same limitation (as did FirstEnergy) under Section 14.2 of the OATT which contains the non-firm priority provisions. With this modification, the service is consistent with pro forma tariff and our actions in FirstEnergy.

7. Miscellaneous Issues

Section 27.1 of the Alliance OATT addresses cost responsibility for network upgrades associated with new generation. Alliance Companies state that Alliance will identify locations on the transmission system where new generation facilities would be beneficial to the network and/or can be accommodated without significant network upgrades. Transmission customers requesting to connect generation facilities at other locations will be required to pay the cost of network upgrades to accommodate the new generation. If Alliance requires the construction of network upgrades that cannot be directly assigned to specific transmission customers, Alliance will develop, and file with the Commission, a mechanism to allow transmission owners constructing the facilities to recover the full annual revenue requirement associated with the facility, or the costs of upgrades not completed despite the exercise of due diligence. Alliance Companies argue that this provision is necessary to ensure that Alliance has adequate incentives for constructing new facilities.[173]

Coalition argues that the proposal: (1) is unreasonable under the proposed rate design because increases in load will automatically provide additional revenues to pay for network upgrades; (2) would directly assign costs that do not qualify for direct assignment under existing Commission policies; (3) does not provide a credit if other transmission customers use the network upgrade; (4) does not give customers that paid for the network upgrades priority rights to use capacity; (5) may lead to discriminatory treatment of generators as Alliance will be charged with identifying such locations on the system; and (6) lacks a mechanism to group together expansion projects which may be more economical from a regional perspective rather than incremental expansions. Coalition requests that the expansion adder be rejected or in the alternative, a revenue credit tracker be adopted. [174]

In Order No. 2000,[175] the Commission stated that it was appropriate to provide flexibility for pricing of new facilities and indicated that proposals for pricing of new facilities that combine elements of incremental prices with embedded-cost access fees would be considered. We find that Alliance Companies' proposal is consistent with Order No. 2000. However, Coalition raises, among other things, issues regarding credits associated with other customers' use of the upgrade, and transmission rights that are not addressed in Alliance Companies' proposal. We note that Alliance Companies, in their answer, propose to hold an informal technical conference regarding Alliance's generator interconnection procedures, and we direct the parties to address these and other related issues at that conference. We will address any remaining issues when Alliance Companies file their revised procedures.[176]

Finally, numerous intervenors have raised issues regarding certain typographical errors, omissions and stylistic concerns regarding changes from the pro forma tariff. [177] Additionally, intervenors express concerns that certain preexisting obligations and commitments be carried over and honored by Alliance. [178] We direct Alliance Companies to address these concerns in their compliance filing to this order and to the extent that issues remain, we will address them at that time.

C. Generator Interconnection Procedures and Pro Forma Interconnection Agreement

1. Alliance Companies' Proposal

Alliance Companies include interconnection procedures and a pro forma interconnection agreement as Attachment U to the Alliance OATT, which detail the terms and conditions of generation interconnection. Alliance Companies state that they are currently exploring mechanisms to provide generation-based ancillary services at market rates and expect to include such a proposal into their compliance filing. In the meantime, Alliance Companies state that they have proposed adequate provisions which will enable Alliance to provide, by procurement, ancillary services from interconnected generators and control area operators. [179] Alliance Companies explain that they will require all generators interconnected to its transmission system to execute a generator interconnection agreement with Alliance. [180] Under this agreement, generators will be required to supply the necessary ancillary services, as determined by Alliance, until it makes a determination that sufficient third-party supply is available through a regional power exchange or other means. Under Alliance's Operating Protocol, Alliance may also designate certain generating units as must-run units.

2. Intervenors' Comments

Consumer Advocates argue that the generator interconnection procedures create unnecessary obstacles to small distributed and renewable generation. [181] Consumer Advocates argue that the procedures are so broadly drafted that it will stunt the growth and development of small scale generators on the Alliance system. Consumer Advocates also note that PJM has fewer restrictive procedures for small interconnections of under 10 MW, and requests that the Commission require Alliance Companies to modify their proposal accordingly. Public Interest Organizations agree that the interconnection provisions should be modified to include the addition of de minimus standards for very small generators and an expedited process for generators less than 10 MW. [182] Indicated Parties filed an untimely motion for clarification, conditional protest, and request for a technical conference that raises numerous issues regarding the pro forma interconnection agreement. Indicated Parties also ask the Commission to clarify that this order will not constitute a determination that the proposed OATT provisions are just and reasonable or otherwise consistent with the FPA or Order No. 2000, so as to impair parties' ability to challenge the OATT as part of Alliance Companies' January RTO filing. Indicated Parties assert that if their motion for clarification is granted their protest will be moot, but if the Commission denies their motion for clarification Indicated Parties seek leave to file their instant protest. Tenaska protests that the interconnection procedures go beyond what is appropriate in the context of this compliance filing and, in any event, contain several questionable provisions including the definition of system upgrades, crediting mechanisms, negotiation procedures, and ownership rights. Tenaska supports Indicated Parties' request for a technical conference.

3. Alliance Companies' Answer

Alliance Companies respond that the interconnection agreement and procedures are consistent with those approved by the Commission in Entergy Services, Inc., 91 FERC ¶ 61,149 (2000) (Entergy) and American Electric Power Service Corp., 91 FERC ¶ 61,308 (2000). Alliance Companies note that the agreement and procedures apply to generators that serve wholesale power customers, and do not apply to generation behind the meter not used to engage in wholesale transactions. [183] Alliance Companies also filed an answer to Indicated Parties' motion for clarification or technical conference, and conditional protest. Alliance Companies do not oppose deferring action on the interconnection agreement and procedures until such time as they are submitted as part of their Section 205 OATT filing. [184] Although Alliance Companies oppose Indicated Parties' alternative request for a technical conference, Alliance Companies commit to host

an informal conference with interested parties to discuss issues relating to the interconnection agreement and procedures well before making their Section 205 OATT filing. [185]

4. Discussion

We will grant Indicated Parties' motion for clarification, as discussed below. We again take this opportunity to remind parties that our silence on any particular issue does not indicate acceptance or a determination under the FPA or Order No. 2000. Our intention is to provide as much guidance as possible to assist Alliance Companies in making a full and complete RTO filing. Therefore, we have limited our rulings to specific areas in which Alliance Companies have attempted to comply with the Alliance I and II Orders, e.g., rate pancaking, independence and redispatch. We do note, however, that considerable resources have been expended by the parties and the Commission on what is now the third Alliance filing. Therefore, we expect that all parties, including Alliance Companies, adhere to the guidance we have provided in this order so that many of the issues raised here will either be resolved or narrowed when Alliance Companies make their compliance filing and subsequent compliance filing to this order. We also strongly encourage the parties and Alliance Companies to resolve their differences regarding the interconnection agreement and procedures at the informal conference which Alliance Companies will host.

We will defer action on Alliance Companies' proposed interconnection procedures and pro forma interconnection agreement pending Alliance Companies' commitment to file them under Section 205. However, we note that there are inconsistencies among Alliance Companies' Operating Protocol, Planning Protocol, OATT, and their answer regarding exceptions for small generators. For example, Alliance Companies state in their answer that the interconnection agreement and procedures apply to generators that serve wholesale power customers, but they do not apply to generation units "behind the meter" that are not used to engage in wholesale transactions. [186] Nevertheless, Attachment U, Generator Interconnection Procedures and Agreement under the OATT does not contain any exception, [187] and "Generator"is defined broadly to encompass generation entities connected to Alliance. [188] Moreover, we note that Section 12.1.2 of the Operating Protocol requires that "any generator" connecting with Alliance must sign the interconnection agreement and comply with the interconnection procedures. Therefore, we direct Alliance Companies to clearly provide an exception for small generators in their Section 205 filing. [189] Finally, we direct Alliance Companies to file their must-run agreements, which they failed to include in this filing.

VI. Consumers' Alternative Governance Structure, Docket Nos. ER00-2869-000 and EC00-103-000

A. Consumers' Filing

On June 16, 2000, Consumers sought Commission approval of an alternative governance structure (Structure B) for Alliance in Docket Nos. ER00-2869-000 and EC00-103-000. Consumers states that the alternative governance structure is identical to its proposal filed in Docket No. ER99-3144-000. Consumers argues that while the Alliance I Order dealt with central aspects of Alliance Companies' governance proposal, it did not address Consumers' governance proposal or rule on any aspect of the proposal. Consumers states that under Consumers' Structure B proposal: (1) Alliance Companies would directly hold 49 percent of Alliance Transco at and after formation; (2) a newly-created public utility holding company, Publico, will hold 51 percent of Alliance Transco at formation (but could purchase greater interests as its market capitalization also grew over time); (3) each market participant, including each Alliance Company, would be able to hold 1 percent interest in Publico, in addition to the Alliance Companies' direct interests in Alliance Transco; and (4) Alliance Companies would hold one or more seats on a newly-created Alliance Transco Board of Directors.

Consumers asks that the Commission authorize Structure B under the RTO standards only. According to Consumers, if Structure B is not accepted by the Commission, Consumers will evaluate whether to exit Alliance.

B. Notice of Filing, Interventions, and Consumers' Answer

Notice of Consumers' filing was published in the Federal Register, 65 Fed. Reg. 41,969 (2000), with comments, protests, and interventions due on or before July 17, 2000.

Intervenors who protest the filing generally claim that Consumers' Structure B proposal would vest Alliance Companies with even more direct and indirect control over Alliance Transco than would the original Alliance proposal addressed in the Alliance I and II Orders. Intervenors who protest the filing uniformly ask the Commission to reject the filing as inconsistent with the requirements for corporate governance stated in Order No. 2000 and the Alliance I and II Orders.

Intervenors who protest express particular concern that Consumers' Structure B proposal will allow Alliance Companies to control, at formation, 49 percent of the voting

equity interests in Alliance. Intervenors state that this figure represents a significant threat to the independence of Alliance, and further note that the figure substantially exceeds the Commission's 15 percent benchmark for class ownership.

Coalition disputes each of Consumers' assertions, and argues that Consumers is collaterally attacking Order No. 2000 through this filing. Joint Consumer Advocates and Midwest Customers also state that the Structure B proposal fails to comply with the State of Michigan's state restructuring law.

On July 31, 2000, Consumers moved for leave to answer the protests. Consumers argues that the Commission has no legal authority to establish ownership limitations for RTOs or to regulate the corporate structures of jurisdictional companies, whether or not those companies are RTOs. Consumers denies that Structure B will provide Alliance Companies with control over Alliance. Consumers also asserts that: (1) Order No. 2000 places no upper limit on RTO ownership; (2) Consumers' structure B proposal satisfies Order No. 2000's independence requirements; (3) Consumers' obligation under Michigan law to join an RTO is not relevant to our consideration of its Structure B proposal; and (3) the Commission invited Consumers to make this filing.

C. Discussion

1. Procedural Matters

Under Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2000), the timely notice of intervention of Michigan Public Service Commission and the timely, unopposed motions to intervene by intervenors listed in Appendix B serve to make them parties to this proceeding. Given the early stage of this proceeding, their interest in the proceedings, and the absence of any undue prejudice or delay, we find good cause to grant the untimely motions to intervene of Dynegy and Norton Energy. Notwithstanding Rule 213(a)(2) of the Commission's Rules of Practice and Procedure (see18 C.F.R. § 385.213(a)(2) (2000)), which generally prohibits an answer to a protest, we will accept Consumers' answer given the complex nature of this proceeding and because the answer aided in clarifying certain issues.

2. Consumers' Filing

We find that Consumers' assertion that the Commission does not have jurisdiction over the proposed corporate structure over RTOs is plainly incorrect. In Order Nos. 2000 and 2000-A, we specifically discussed at length our legal authority with respect to this

issue. We find that Consumers' argument in this regard is a collateral attack on Order Nos. 2000 and 2000-A, which we will not entertain further in this proceeding.

In addressing the merits of Consumers' proposal we note that in the Alliance I and II Orders and Order No. 2000, we explained at length our rationale for requiring that the corporate governance of an RTO be independent from market participants. We find that Consumers' Structure B proposal does not comply with those orders. Under Alliance Companies' governance proposal, which the Commission rejected, Alliance Companies would have directly owned 5 percent each (a total of 25 percent) of Alliance Publico, and would have exercised "passive" control over Alliance Transco. Under Consumers' Structure B proposal, Alliance Companies would directly hold 49 percent of Alliance Transco at and after formation. A newly-created public utility holding company, Publico, would hold 51 percent of Alliance Transco at formation, but could purchase greater interests as its market capitalization also grew over time. Therefore, we find that Consumers' Structure B proposal exhibits an even greater and more direct degree of utility control over Alliance than that exhibited by the prior Alliance Companies' proposals. Therefore, we will reject Consumers' Structure B proposal.

VII. Requests for Rehearings

Consumers and Coalition filed timely requests for rehearing of the Alliance II Order.

A. Consumers' Request for Rehearing

Consumers complains that the Alliance II Order did not rule on Consumers' proposal for an alternative governance structure (Structure B) for Alliance. [190] As explained above, we are rejecting Consumers' alternative governance proposal because it allows even more utility company control over the proposed Alliance than Alliance Companies' own proposal. Consequently, we will deny Consumers' rehearing request.

B. Coalition's Request for Rehearing

In Coalition's request for rehearing of the Alliance II Order, it argues that the Commission did not decide issues concerning Alliance Companies' designation of facilities to be transferred to the functional control of Alliance. [191] Coalition also filed a conditional motion for reconsideration of the Alliance I Order requesting that the Commission: (1) state that all issues concerning the scope of transmission facilities to be transferred remain open; (2) require additional procedures to determine issues concerning

the scope of such facilities; and (3) clarify that Alliance Companies retain the burden of proof with respect to all unresolved issues relating to such facilities.

We will deny Coalition's request for rehearing and motion for reconsideration. In the Alliance I and II Orders we addressed issues concerning the transfer of facilities to the extent necessary to ensure compliance with then-governing ISO principles and to enable Alliance to commence operations. In the Alliance I Order, we conditionally approved Alliance Companies' proposed list of facilities to be transferred to the functional control of Alliance. We found that Alliance Companies' proposal satisfied ISO Principle No. 5 requiring control over the operation of interconnected transmission facilities within the region. The Alliance I Order noted that exercise of functional control - as opposed to direct operational control - is an appropriate method of providing control of an ISO's transmission system. [192] Under Order No. 2000, we permitted RTOs to determine the best division between direct and functional control. [193] We now clarify that our conditional approval did not extend to any other facilities. In the Alliance II Order the Commission specifically stated in response to a rehearing request that Alliance Companies continue to bear the burden of proof concerning any aspect of their proposal not accepted in the Alliance I Order. [194]

Furthermore, we emphasized in the Alliance I Order that our initial approval of Alliance Companies' proposed filing, including the transfer of facilities, was conditional under Order No. 888's ISO principles. This was and is appropriate because Alliance remains under development and must now also satisfy the requirements of Order No. 2000. Thus, we believe that it would be premature to require additional data or fact-finding procedures requested by Coalition since the final form and structure of Alliance is as yet undetermined. Nonetheless, we clarify that the previous Alliance I and II Orders did not decide any other issues, except as referenced above, concerning the transfer of facilities.

We direct Alliance Companies to list facilities that will be transferred when they make their compliance filing. This will provide an additional opportunity for parties to recommend any changes they believe are appropriate. To the extent possible, however, we encourage Alliance Companies to undertake discussions with concerned parties on these issues before this RTO filing. Finally, we note that after Alliance commences operations, it may become necessary to review the need for transfer of additional facilities.

The Commission orders:

(A) Alliance Companies' compliance filing is hereby accepted to the extent discussed in the body of this order, and Alliance Companies are directed to submit further filings as discussed in the body of this order.

(B) Alliance Companies are directed to file their actual rates no later than 120 days prior to the commencement of operations.

(C) Consumers' alternative governance structure filed in Docket Nos. ER00-2869-000 and EC00-103-000 is hereby rejected.

(D) Consumers' and Coalition's requests for rehearing are hereby denied as discussed in the body of this order.

(E) Alliance Companies are directed to take part in the settlement judge procedures established in Docket No. ER01-123-000.

(F) The Commission's Dispute Resolution Service is directed to convene a meeting of the parties to address grandfathered contracts within 45 days after the date this order issues.

(G) Alliance is directed to report to the Commission on the status of the negotiations by December 31, 2003 as discussed in the body of this order.

(H) As discussed in the body of this order, Alliance Companies are hereby directed to file their compliance filing, which will also constitute the supplement to their January 16 filing, no later than May 15, 2001.

By the Commission. Commissioner Massey dissented with a separate statement attached.

(S E A L)

David P. Boergers,
Secretary.

Appendix A

Listed parties have filed notices of intervention or motions to intervene in Docket Nos. ER99-3144-004 and/or EC99-80-004. Short-hand references to parties referred in the order are indicated in parenthesis after the name. Late interventions are indicated by an asterisk.

Company Name

Allegheny Energy Service Corporation
(Allegheny Energy)
American Municipal Power-Ohio, Inc.
(AMP-Ohio)
American Public Power Association and
National Rural Electric Cooperative
Association (APPA & NRECA)
Buckeye Power Inc. and Ohio Rural
Electric Cooperative (Buckeye)
Chaparral (Virginia), Inc. (Chaparral)
Citizen Power, Inc. (Citizen Power)
Citizens Action Coalition of Indiana, Inc.,
Izaak Walton League of America, Inc.,
Midwest Office and Environmental Law and
Policy Center of the Midwest
(Public Interest Organizations)
Coalition of Midwest Transmission
Customers (Midwest Customers)
Coalition of Municipal and Cooperative
Users of Alliance Companies'
Transmission (Coalition)
Coral Power, L.L.C. (Coral)*
Electricity Consumers Resource Council,
American Iron and Steel Institute, and
American Chemistry Council
(Industrial Consumers)
Enron Power Marketing, Inc. (Enron)
Illinois Commerce Commission
(Illinois Commission)
Indiana Office of Utility Consumer Counselor
International Transmission Company
Maryland Office of People's Counsel
Midwest ISO Participants (Midwest ISO)

North Carolina Electric Membership
Corporation (NCEMC)
Ormet Primary Aluminum Corporation (Ormet)
PG&E National Energy Group, Inc.*
PJM Interconnection, L.L.C. (PJM)
Pennsylvania Office of Consumer Advocate
Delaware Public Advocate
Illinois Citizens Utility Board
Indiana Office of Utility Consumer Counselor
Maryland Office of People's Counsel
The Attorney General of Michigan
Missouri Office of the Public Counsel
Ohio Consumers' Counsel
West Virginia Consumer Advocate Division
(Consumer Advocates)
Pennsylvania Public Utility Commission
State of Michigan
Michigan Public Service Commission
Public Utilities Commission of Ohio
Indiana Utility Regulatory Commission
(State Commissions)
Public Service Electric and Gas Company
(PSE&G)
Shell Energy Services Company, L.L.C.
Steel Dynamics, Inc. (Steel Dynamics)
Tenaska, Inc. (Tenaska)*
Virginia State Corporation Commission
(Virginia Commission)
Wabash Valley Power Association, Inc.
(Wabash Valley)
Wolverine Power Supply Cooperative, Inc.
(Wolverine)

Listed parties have filed notices of intervention or motions to intervene in Docket Nos. EC00-103-000 and/or ER00-2869-000. Short-hand references to parties referred in the order are indicated in parenthesis after the name. Late interventions are indicated by an asterisk.

Company Name
AMP-Ohio
Blue Ridge Power Agency
  Central Virginia Electric Cooperative
  Craig-Botetourt Electric Cooperative
  Old Dominion Electric Cooperative
  Virginia Municipal Electric Association No. 1
  ElectriCities of North Carolina, Inc.
  Orangeburg Department of Public Utilities
  Indiana Municipal Power Agency
  Michigan Public Power Agency
  Michigan South Central Power Agency
  Detroit Public Lighting Department
  City of Dowagiac
  City of Sturgis
  City of Wyandotte
  (Coalition)
Citizen Power
Consumer Advocates
Dynegy Power Marketing, Inc.*
Indiana Office of Utility Consumer Counselor
Michigan Public Service Commission*
Midwest Customers
NCEMC
Norton Energy Storage, LLC*
Virginia Electric & Power Company
Wabash Valley

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Alliance Companies	Docket Nos. ER99-3144-003, ER99-3144-004, ER99-3144-005 and RT01-88-000
American Electric Power Service Corporation on behalf of: Appalachian Power Company Columbus Southern Power Company Indiana Michigan Power Company Kentucky Power Company Kingsport Power Company Ohio Power Company Wheeling Power Company	Docket Nos. EC99-8--003, EC99-80-004, and EC99-80-005
The Detroit Edison Company	
First Energy Corporation on behalf of: The Cleveland Electric Illuminating Company Ohio Edison Company Pennsylvania Power Company The Toledo Edison Company	
Virginia Electric and Power Company	
Consumers Energy Company	Docket Nos. ER00-2869-000 and EC00-103-000 (not consolidated)

(Issued January 24, 2001)

MASSEY, Commissioner, dissenting:

I am issuing the same dissent to this order and today's order in Illinois Power, Docket No. ER01-123, due to the common issues addressed.

I must dissent from the decision in the Alliance order to accept the proposed scope and configuration of the Alliance Companies. In two prior orders, the Commission

expressed strong concern with the Alliance scope and configuration. In the latest filing, Alliance has done little to improve its scope beyond informing the Commission that two additional small transmission owners intend to join Alliance and that it is working on seams management agreements with other transmission organizations. Nevertheless, today's order now accepts the proposed scope. I suppose, as they say, "the third time is the charm." But I respectfully disagree. An organization shaped more or less like a snake that stretches from the Great Lakes to the Mid-Atlantic does not satisfy the scope and configuration characteristic that I voted for in Order No. 2000. As our prior orders have said, the Alliance organization separates buyers and sellers that constitute predominant west to east trading patterns and can act as a strategically located toll gate. I am very disturbed by the precedent today's order sets for future RTO development.

With today's order, one of my greatest concerns regarding the Commission's evolving RTO policy is borne out. Our original Alliance order found that Alliance Companies' proposed scope and configuration raised concerns and held out the possibility that Alliance, PJM and the Midwest ISO could negotiate procedures that would address scope issues.[1] Alliance's first compliance filing did little to change the scope and configuration and stated only that the companies were addressing seams issues with neighboring control areas. Our order addressing that compliance filing reserved judgment pending further filings.

In a concurrence to that order, I held that the Commission missed an important opportunity to provide much needed guidance regarding scope and configuration, and expressed my concern that we may have erroneously implied that seams management agreements are an acceptable substitute for adequate scope and configuration.[2]

Today's order unfortunately confirms that the implication I feared was in fact not erroneous. Here, the majority elevates seams management agreements to the status of a complete substitute for the basic characteristic of adequate scope and configuration. This is a significant mistake, and continues a flawed policy evolution that eviscerates a core feature of Order No. 2000.

In addition to their many important pro-competitive features, well shaped Regional Transmission Organizations offer the potential to enhance reliability. This is a critical rationale for the RTO. A single RTO responsible for the grid over a large and

appropriately shaped area can enhance reliability through centralized regional responsibility for loop flow, congestion management, regional redispatch, coordination during system emergencies and restorations, conducting comprehensive reliability studies, coordination of transmission and generation outage schedules, sharing ancillary service responsibilities, and providing one-stop shopping for new generators over a broad market area.

Realizing these valuable reliability benefits requires an RTO with the proper scope and configuration. In other words, the actual shape of the RTO is important to reliability. Managing loop flow across a broad region, for example, requires a shape that can generally internalize the bulk of the loop flow. Reliability-enhancing scope and configuration is something we have yet to see from the Alliance Companies.

I am very skeptical that mere seams agreements with neighboring control areas will be capable of addressing all inadequacies of the proposed scope and configuration. If seams management agreements were sufficient, there would be no need for any scope and configuration requirements at all. Yet, achieving the reliability and other benefits of RTOs depends on the ability of the RTO to control all of the transmission facilities in an appropriate region. This is not accomplished by coordination agreements with neighboring entities. Every seam, even if addressed by an agreement, is a potential bump in the road. The more seams arising from too small or from poorly configured entities, the more dysfunctional the market. Order No. 2000 does indeed include a requirement for interregional coordination as RTO Function No. 8. But this function was never intended to be a substitute for adequate scope and configuration. What was intended is that once there is an RTO of appropriate shape and adequate scope and configuration, Function 8 requires the RTO to coordinate with other appropriately configured RTOs.

I would have strongly preferred to defer a merits call on Alliance's scope in this order. I would have directed Alliance to participate in the discussions the Commission establishes in the companion Illinois Power case with the clear objective of a single RTO for the Midwest. It is my goal that the parties find common ground in an RTO that embraces both the Alliance transco and the Midwest ISO. A single RTO could then come back to the Commission with an adequate scope and configuration, and the region could have had the single RTO that it needs for truly seamless trading. Virtually every intervenor in this case, including numerous state commissions, argues for a single RTO for the Midwest.

I would suppose that mere seams agreements will be the objective in the negotiations. Given the current flux of Midwest ISO membership, I have to wonder which seams Alliance will address and with whom. Today's order puts the cart before

the horse. Stated more bluntly, today's order eliminates scope and configuration from the requirements of Order No. 2000. After today, any RTO of meager size, odd shape, and poor configuration can meet our standards for RTOs.

I must also dissent from today's order in Illinois Power. In this case, Illinois Power requests our authorization for withdrawal from the Midwest ISO. The state of RTO formation in the Midwest is in a serious state of uncertainty and chaos. There has been a steady stream of transmission owners seeking to abandon the Midwest ISO. This state of flux has been caused in large measure by the Illinois Power and Commonwealth filings. Some transmission owners have even said that their desire to leave Midwest ISO is due to these withdrawals and their effect on the ISO's scope and configuration. They have no interest in abandoning the Midwest ISO, but also have no interest in remaining in an RTO that is composed, after defections, of gaping holes and utility islands. Clearly we need to act on this matter as soon as possible in order to restore order to RTO formation in the Midwest region of the country.

I agree with the order's decision to hold in abeyance a decision on Illinois Power's request and to require the parties to this case to attempt to negotiate a resolution to the membership controversy now engulfing the Midwest ISO. And I believe those negotiations should occur under the Commission's settlement judge procedures. Where I disagree with today's order is in the vague guidance given to the settlement judge regarding the objective of the negotiations.

The negotiations we order today should clearly direct stakeholders in the Midwest to forge a single RTO for the region. I say this for three reasons. First, and foremost, the Midwest region is too small for two RTOs. It's just that simple. The geographic area encompassed by the Alliance and the Midwest RTO is the proper scope for one RTO. We've had a number of parties in these filings, including virtually every state commission in the region, tell us that the goal should be a single RTO. Those state commissions are Ohio, West Virginia, Indiana, Michigan, Iowa, Pennsylvania, and Illinois.

The second reason is that a single RTO is a reasonable and achievable goal. Much has changed since the initial formation of the Midwest ISO and Alliance. Attitudes toward business models have evolved, and this Commission has set out some guidance on how hybrid organizations can fit within the Order No. 2000 framework. For example, the parties can organize one RTO for the Midwest region that accommodates both the transco and ISO organizational models within it. The Commission has demonstrated flexibility in allowing hybrid organizations to accommodate the need or

desire for different ownership forms.[3] We have also received at least one RTO proposal that accommodates both the transco and ISO organizational forms. I am referring to the RTO West proposal.[4]

I think we are missing a golden opportunity now. The settlement judge has no clear guidance on how to focus the negotiations. It's very unclear what we will get reported back to us, but it is likely to be either nothing or a mere seams agreement between two poorly shaped RTOs. Our target date for RTO operation is drawing ever near. Through our imprecision, perhaps driven by lack of will, we fail to act decisively and place at risk RTO formation in the Midwest.

For these reasons, I dissent from both of these orders.

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William L. Massey
Commissioner