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Client Alert

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FERC Issues Proposed Rulemaking to Revise the *Avista* Policy on Ancillary Services, and Adopt a New Policy on Waivers of Accounting and Reporting Requirements

The Federal Energy Regulatory Commission (FERC) recently issued a Notice of Proposed Rulemaking (the NOPR) that contemplates revisions to its decade-old *Avista* policy, which restricts sales of ancillary services at market-based rates outside organized markets. In order to narrow the applicability of the stringent *Avista* restrictions, the NOPR proposes a variety of ways for sellers to justify market-based rate sales of ancillary services outside organized markets, including allowing such sales when the seller passes the market power screens for sales of energy and capacity, and establishing new screens specifically for ancillary services. In addition, the NOPR proposes cost-based mitigation methods for sellers that do not pass the applicable market power screens.

In the same NOPR, FERC proposes to amend its accounting and reporting requirements to better account for the use of energy storage devices in public utility operations. These proposed amendments reflect FERC's determination that existing accounting and reporting requirements do not provide sufficiently transparent information about the activities and costs of new energy storage operations. The proposed amendments also include one change, apparently applicable not only to storage providers but to public utilities more generally, that market-based rate sellers seeking recovery of a portion of their costs under cost-based rates be required to forego previously-granted waivers of FERC's accounting and reporting requirements.

Proposed Revisions to the *Avista* Policy

In the 1999 *Avista* case, FERC found data limitations impaired the ability of sellers to perform traditional market power screens for ancillary services. In the hope of facilitating market-based rate sales of ancillary services outside organized markets, FERC adopted a policy allowing third-party ancillary service providers to sell certain ancillary services at market-based rates subject to three restrictions. Specifically, sellers cannot make sales of ancillary services at market-based rates to (i) an RTO or ISO with no ability to self-supply ancillary services; (ii) a traditional, franchised public utility affiliated with a third-party supplier, or sales where the underlying transmission service is on the system of the public utility affiliated with the third-party supplier; or (iii) a public utility that is purchasing ancillary services to satisfy its own Open Access Transmission Tariff (OATT) requirements to offer ancillary services to its own customers.

In an effort to foster the development of a competitive ancillary services market, FERC issued a Notice of Inquiry in 2011 seeking comment on whether revisions affecting the scope of the final *Avista* restriction were appropriate. Based on feedback received in response to the Notice of Inquiry, FERC put forward the package of proposals found in the NOPR.

The NOPR seeks comments on various issues related to market-based rate sales of ancillary services. The first three involve proposals to provide sellers with alternative means to demonstrate that they lack market power.

- FERC proposes to revise its regulations to include a rebuttable presumption that sellers that pass the traditional market power screens used in authorizing sales of energy and capacity at market-based rates also lack horizontal market power as to energy imbalance and generator imbalance services. FERC requests comments on the proposal, including comments on any unique technical requirements or limitations that might be relevant.

- The NOPR notes that there seem to be technical limitations for ancillary services other than imbalance service that make the traditional market power screens inadequate to determine whether horizontal market power exists. FERC seeks comments on whether the technical requirements for operating reserve-spinning, operating reserve-supplemental, reactive supply and voltage control, and regulation and frequency response would necessitate a market-power analysis based on a different geographic market or a different set of resources as compared to those analyzed under the traditional market power screens.

- FERC proposes allowing an optional market power screen for ancillary services that will compare the amount of capacity that a potential seller can dedicate to providing the ancillary service in the relevant geographic market with a transmission provider's aggregate requirement for the ancillary service in the market. In order to permit sellers to develop the market power screen, FERC also proposes to require each public utility transmission provider to publicly post on its OASIS information on the aggregate amount of ancillary service that it has historically required, including any geographic limitations it may face in meeting those requirements. FERC seeks comment on the optional market power screen and the appropriate level of detail to include in the reporting requirements.

The NOPR also requests comments on cost-based mitigation measures to ensure just and reasonable rates for third-party sales of regulation and frequency response, operating reserve-spinning, or operating reserve-supplemental by sellers that have not demonstrated a lack of market power. These mitigation measures would only be an alternative to the third restriction in *Avista*, which involves sales to a public utility that is purchasing ancillary services to satisfy its own OATT requirements to offer ancillary services to its own customers.

- The NOPR proposes two price cap alternatives. The first option is a rate not to exceed the buying transmission provider's existing OATT rate for the same ancillary service. The second option is a rate not to exceed the highest public utility transmission OATT rate within the relevant geographic market for physical trading of the ancillary service in question. FERC seeks comments on the two price cap proposals, and the utility of such a price cap to sales of reactive supply and voltage control.

- The NOPR also proposes to allow public utilities to seek a waiver from the final *Avista* restriction by relying on competitive solicitations meeting FERC's requirements. FERC proposes that entities filing for such a waiver demonstrate that the solicitation attracted sufficient seller interest to properly discipline market prices. FERC seeks comments on the proposal and ideas on ways in which solicitations can be structured to accommodate near-term transactions.

Accounting and Reporting Requirements

The NOPR also addresses FERC's accounting and reporting requirements for energy storage operations. Because energy storage assets can have operating characteristics consistent with production, transmission, and distribution of electric energy, the possibility exists that they could provide multiple services and could simultaneously recover costs under both cost-based and market-based rates. After reviewing comments on the Notice of Inquiry, FERC determined that current accounting and reporting requirements do not provide sufficient transparency concerning storage operations. The NOPR does not propose to create a new functional classification for energy storage, because FERC believes that existing functional classifications can adequately support energy storage operations. The NOPR proposes the following changes to the Uniform System of Accounts, Form Nos. 1, 1-F, and 3-Q in order to provide transparent information on the activities and costs of new energy storage assets:

- Amendment of FERC's Uniform System of Accounts to add a new electric plant and operating and maintenance expense accounts to record the installed cost and operating and maintenance cost of energy storage assets, and a new account to record the cost of power purchased for use in energy storage operation;

- Amendment of Forms 1 and 2-F to include new accounts and amended schedules to report statistical and operational information on energy storage operations; and

- Amendment of a schedule of Form No. 3-Q to include the new account to record the cost of power purchased for use in energy storage operations.

Notably, the NOPR also proposes that a public utility with market-based rate authority seeking recovery of any service under cost-based rates forego its waivers of FERC's accounting and reporting requirements. This proposal would appear to apply to all public utilities, not just those with storage operations. The NOPR seeks comment on whether there should be some threshold for cost-based recovery (*e.g.*, more than 10 percent) or other trigger for losing these waivers.

Comments on the NOPR are due 60 days after its publication in the *Federal Register*.