

of the transaction. The Commission also stated that the seller should explain how fractional allowances will be handled, and suggested a "rounding" approach, *i.e.*, rounding up to the next whole number if the fraction is greater than one-half, or down if the fraction is less than one-half. Finally, the Commission stated that the ratemaking treatment of emissions allowance costs endorsed in the Policy Statement does not preclude other approaches proposed by individual public utilities on a case-by-case basis.

In the Interim Rule (codified in § 35.23 of its regulations), the Commission stated that if public utilities have rate schedules on file that expressly provide for the recovery of all incremental or out-of-pocket costs, these utilities may make abbreviated rate filings, limited to detailing how they would recover emissions allowance costs. Regarding coordination rates that do not provide for the recovery of all incremental costs, the Commission concluded that the public utility may include rate schedule amendments together with the abbreviated filing if customers agree to the rate change; if the customers do not agree to revise such rates, the Commission stated that the public utility must tender its emissions allowance proposal in a separate section 205 rate filing, fully justifying its proposal.

In a separate order disclaiming jurisdiction,⁵ the Commission concluded that emissions allowances are not facilities subject to the Commission's jurisdiction under section 203. The Commission further concluded that a sale or transfer of emissions allowances does not require a filing under section 205 when that sale or transfer occurs outside of a sale by a public utility for resale in interstate commerce.

The Commission invited interested persons to submit additional written comments on the matters addressed in the Interim Rule by January 23, 1995. EEI, Illinois Power and the Pennsylvania Commission timely submitted comments. As explained in greater detail below, EEI and Illinois Power suggest clarification of the Policy Statement provision regarding timing. Illinois Power also suggests clarification of the Policy Statement and Interim Rule regarding the use of indices.⁶

an emissions allowance equivalent in the following year, plus other possible punishments depending on the degree of violation. *Id.* at 31,201.

⁵ Edison Electric Institute, 69 FERC ¶ 61,344 (1994).

⁶ Illinois Power also refers to the findings in the Policy Statement and Interim Rule regarding the calculation of the amount of emissions allowances

The Pennsylvania Commission request clarification of the Interim Rule to state that the Rule applies to jurisdictional rates only, and does not contemplate preemption of the states' ratemaking treatment of emissions allowances.

IV. Discussion

A. Timing

EEI and Illinois Power maintain that the Policy Statement, as issued, could be construed to give customers the option of waiting until the "true-up" date to declare whether they will pay or return emissions allowances in kind.⁷ Thus, EEI argues, utilities might not know how many allowances the customers would return until it is too late to avoid incurring EPA penalties.⁸ EEI maintains that to assure that they have sufficient emissions allowances on hand, and thus avoid penalties, utilities would have to either: (1) tie up their own capital to create an allowance reserve, or (2) be prepared to purchase allowances at the last minute, possibly paying a premium in the form of a scarcity rent. To remedy this situation, EEI suggests clarifying the Policy Statement to state that utilities may require customers, to declare, at or near the time of the coordination transaction (or earlier), whether they will pay or return emissions allowances in kind, and, if they return allowances in kind, the time at which they will do so.⁹

EEI further notes the public utilities face risks associated with the timing of the return of allowances in kind, including: (a) the risk that if a sale is arranged by a power broker or marketer, that entity may become insolvent and not deliver allowances; and (b) the risk

associated with a coordination transaction and reconciliation of inconsistencies in dispatch criteria, but does not suggest any modifications to these findings.

⁷ Illinois Power notes the Commission's order in Southern Company Services, Inc., 69 FERC ¶61,437 (1994), *reh'g pending*, in which the Commission, consistent with the Policy Statement and Interim Rule, directed the Southern Companies to modify their submittal to allow customers that choose to return allowances in kind to do so up to the EPA reporting date rather than at the time of the transaction.

⁸ See *supra* note 4.

⁹ EEI emphasizes that because of EPA's administrative requirements, utilities must have the requisite number of allowances on hand several weeks before the "true-up" deadline. Similarly, Illinois Power argues that providing a utility the option to make an in-kind return of allowances "up to the EPA reporting date," does not necessarily allow for sufficient time to complete a transfer through EPA's Allowance Tracking System. Illinois Power also argues that allowing customers who return allowances in kind to do so up to the EPA reporting date conflicts with payment terms previously established by mutual agreement of the affected parties.

associated with the failure of customers to settle their accounts within the standard billing period. For these reasons, EEI asks the Commission to clarify the Policy Statement to state that utilities may propose arrangements with their customers for indemnification from such risks.

Commission Ruling

In the Policy Statement and Interim Rule, the Commission stated that purchasing utilities that choose to return allowances in kind should be allowed to return the allowances by the appropriate EPA reporting date, rather than at the time of the transaction, *i.e.*, a "timing option." However, if purchasing utilities wait until the time of "true-up" before declaring whether they will pay cash or return emissions allowances in kind, this accords the selling public utilities little, if any, opportunity to determine how many emissions allowances they will need to avoid EPA penalties. To remedy this situation, the Commission will clarify 18 CFR 2.25(e) to state that public utilities may require purchasing utilities to declare, no later than the beginning of the coordination transaction: (a) whether they will pay or return allowances in kind; and (b) if they return allowances in kind, to specify a date by which they will return the allowances.¹⁰ The Commission also will clarify section 2.25(e) to state that public utilities may include, in their agreements, provisions to indemnify themselves if customers do not return allowances when they have declared they will do so.¹¹

B. Use of Indices

Illinois Power argues that the requirement in the Policy Statement and Interim Rule (*see* 18 CFR 2.25(c)) that utilities use the same incremental cost index or indices in pricing coordination sales and in dispatch decisions (or

¹⁰ Such date should afford the selling public utility sufficient time to meet its requirements to EPA. The close of the calendar year would appear to be more than adequate. However, customers should be allowed to designate a date comparable to that which the utility itself would internally designate if it were purchasing allowances to meet its EPA requirements. In other words, the selling utility may not require its customers to provide allowances any earlier than the utility's internal deadlines for purchasing allowances to meet EPA requirements for the prior calendar year. Thus, if the public utility purchases allowances on, for example, January 15, we see no reason to require customers to provide allowances any earlier.

¹¹ Such indemnification provisions should be applied in a non-discriminatory manner. While EEI notes that power marketers and brokers may become insolvent, we note that such entities are not the only entities that may become insolvent; a few traditional utilities have sought bankruptcy protection in recent years.