BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Petition for Expedited Approval of Settlement Agreement with Lake Cogen, Ltd. by Florida Power Corporation	Docket No. 961477-EQ Filed: July 29, 1997

BRIEF OF LAKE COGEN, LTD.

LAKE COGEN, LTD. (hereinafter "Lake" or "Lake Cogen"), pursuant to the Commission's instructions given at its agenda conference on July 15, 1997, hereby files this its brief in support of the petition for approval of the settlement agreement between Lake Cogen and Florida Power Corporation ("FPC") currently pending in this docket.

STATEMENT OF THE CASE AND FACTS

In March 1991, Lake Cogen, Ltd. and Florida Power Corporation entered into that certain Negotiated Contract for the Purchase of Firm Electric Capacity and Energy Between Lake Cogen Limited and Florida Power Corporation (hereinafter "the Contract" or "the Lake Cogen-FPC Contract"). This Contract, along with seven other similar contracts ("the Negotiated Contracts") between FPC and other Qualifying Facilities ("QFs"), was submitted to the Commission for its approval, for cost recovery purposes, in Commission Docket No. 910401-EQ. The Commission approved the Lake Cogen-FPC Contract and the other Negotiated Contracts by its Order No. 24734, which was issued on July 1, 1991. In Re: Petition for Approval of Contracts for the Purchase of Firm Capacity and Energy by Florida Power Corporation, 91 FPSC

7:60.

In August 1994, FPC began implementing a new interpretation of the energy pricing terms of the Contract (and of the other Negotiated Contracts) that resulted in significantly reduced energy payments to Lake Cogen and the other QFs under the Negotiated Contracts. At the same time, FPC filed a Petition for Declaratory Statement with the Commission, later supplemented by an Amended Petition, seeking the Commission's declaration that the disputed energy pricing term in the Negotiated Contracts is consistent with the Commission's rules applicable to energy payments under standard offer contracts. By its Order No. 95-0210-FOF-EQ, the Commission granted the motions to dismiss FPC's petitions filed by Lake Cogen and four other QFs who are parties to the Negotiated Contracts. In Re: Petition for Determination That Implementation of Contractual Pricing Mechanism for Energy Payments To Qualifying Facilities Complies With Rule 25-17.0832, F.A.C., by Florida Power Corp., 95 FPSC 2:263.

FPC's unilateral change in contract interpretation and the resulting reduction in payments resulted in Lake Cogen's filing a lawsuit against FPC, NCP Lake Power, Incorporated, a Delaware corporation, as General Partner of Lake Cogen Ltd., a Florida limited partnership v. Florida Power Corporation, a Florida corporation, Case No. 94-2354-CA01 (hereinafter "Lake Cogen v. FPC"), currently pending in the Circuit Court of the Fifth Judicial Circuit in and for Lake County, Florida. The gravamen of this lawsuit is Lake Cogen's allegation that FPC's new interpretation of the Contract, by which FPC had begun basing

energy payments to Lake Cogen on the basis of computer modeling of a "hypothetical," "contractually defined" avoided unit having only certain limited parameters listed in the Contract for pricing purposes, constituted a breach of the Contract.

On January 23, 1996, pursuant to Lake Cogen's Motion for Partial Summary Judgment, and having heard oral argument on both Lake's Motion and FPC's Cross-Motion for Partial Summary Judgment, the Lake County Circuit Court entered its order granting partial summary judgment in favor of Lake Cogen and against FPC on the issue of liability under the Contract. Specifically, the Court held that FPC is liable under the Contract for "FPC's failure to pay LAKE COGEN at the firm energy cost rate when the avoided unit with operational characteristics of an operable 1991 Pulverized Coal Unit contemplated by the Lake Cogen-FPC Agreement would have been operating and at the as-available energy cost rate during those times when said avoided unit would not have been operating." NCP Lake Power v. FPC, Order Granting Partial Summary Judgment For the Plaintiff and Against the Defendant, Case No. 94-2354-CA-01 (Fla. 5th Circuit, Lake County, January 23, 1996) slip op. at 2-3. FPC did not appeal the Court's decision.

Not long after the entry of the Court's order granting partial summary judgment in favor of Lake Cogen, the parties resumed settlement negotiations. These settlement negotiations eventually resulted in the Settlement Agreement that is the subject of this docket; this Settlement Agreement was executed by the parties on December 5 and 6, 1996 and filed with the

Commission, accompanied by FPC's petition for approval thereof, on December 12, 1996. As averred by Florida Power, and as supported by Lake Cogen, this Settlement Agreement represents an acceptable compromise settlement of the pending dispute and will confer substantial benefits on FPC and its ratepayers. These benefits include reduced payments by FPC to Lake Cogen, substantial curtailment benefits to be provided by Lake Cogen that are not available under the Contract as it presently exists, and a cost-effective "buyout" of the last three years, seven months of the Contract.[1]

The Lake Cogen-FPC Settlement Agreement represents the fifth in a series of similar settlement agreements that FPC has negotiated with QFs who are parties to the Negotiated Contracts. The other four settlement agreements have already been approved, for cost recovery purposes, by the Commission. The most recently approved settlement agreement was between Pasco Cogen, Ltd. and FPC. In Re: Petition for Expedited Approval of Settlement Agreement With Pasco Cogen, Ltd. By Florida Power Corporation, FPSC Order No. 97-0523-FOF-EQ, slip op. (Docket No. 961407-EQ, May 7, 1997). Lake Cogen and Pasco Cogen are affiliated in that subsidiaries of GPU International, Inc. hold 50 percent ownership interests in each partnership. The settlement terms of the Pasco Cogen-FPC Settlement Agreement and the Lake Cogen-FPC Settlement

[1] Pursuant to the buyout, FPC will make certain specified Special Monthly Payments from November 1996 through December 2008, in return for which FPC will be relieved of all payment obligations from January 1, 2010 through July 31, 2013; the latter date is the termination date of the Contract as it presently exists.

Agreement are substantially identical: the energy payment terms under both contracts, as amended by the respective settlement agreements, are identical, and the only differences are that (1) the contract "buyout" pursuant to the Lake Cogen-FPC Settlement Agreement is one year shorter than that pursuant to the Pasco Cogen-FPC Settlement Agreement; (2) the buyout payments are different, corresponding to the different buyout periods; and (3) the Lake Cogen-FPC Settlement Agreement provides significantly greater curtailment benefits for FPC and its ratepayers than does the Pasco Cogen-FPC Settlement.

At its regular agenda conference on June 24, 1997, the Commission adopted, by a 3-to-2 vote, the Primary Staff Recommendation to approve the Lake Cogen-FPC Settlement. The Commission declined to address Issue 1, a legal issue regarding the Commission's authority to deny cost recovery for payments made by utilities under previously approved contracts between QFs and utilities. At its July 15 agenda conference, however, the Commission voted to reconsider its June 24 decision to approve the Lake Cogen-FPC Settlement. The Commission determined to reconsider the issue at its regular agenda conference on August 18, 1997, and permitted the parties to submit briefs addressing Issue 1 as well as the issue whether the Commission's possible refusal to approve the Lake Cogen-FPC Settlement would be inconsistent with, and possibly arbitrary and capricious in light of, its recent approval of the nearly identical settlement between Pasco Cogen, Ltd. and FPC. Lake Cogen respectfully submits this brief addressing these issues.

SUMMARY OF ARGUMENT

The Commission is preempted by federal law from revisiting its approval, for cost recovery purposes, of the Lake Cogen-FPC Contract, and from denying FPC the opportunity to recover payments made pursuant to the Lake Cogen-FPC Contract as it may be interpreted by a court of competent jurisdiction. Moreover, any attempt to revisit the Lake Cogen-FPC Contract, or to deny cost recovery thereunder, would be inconsistent with the Commission's own statements regarding administrative finality of its orders approving contracts between utilities and QFs for cost recovery purposes. Finally, for the Commission to deny approval of the Lake Cogen-FPC Settlement Agreement, where it has previously approved the nearly identical Pasco Cogen-FPC Settlement Agreement, would be contrary to the Florida Administrative Procedure Act and violative of the equal protection guarantees of the Florida and United States Constitutions. For the foregoing reasons, the Commission should not disturb its prior approval of the Settlement Agreement between Lake Cogen and FPC.

ARGUMENT

I. THE COMMISSION CANNOT DENY FPC COST RECOVERY FOR ENERGY PAYMENTS MADE TO LAKE COGEN THAT ARE CONSISTENT WITH THE CONTRACT AS INTERPRETED BY A COURT OF COMPETENT JURISDICTION.

The Commission has inquired into its authority to deny cost recovery of FPC's payments to Lake Cogen pursuant to the Contract between the parties after a Florida court determines that the terms of the Contract require such payments. Lake Cogen

respectfully submits that the Commission has no such authority, and it must allow cost recovery in full. Such action is preempted by the Public Utility Regulatory Policies Act of 1978 ("PURPA"). Moreover, the "filed rate doctrine" precludes any attempt by a state utility commission to impair a utility's right to cost recovery under its contracts with QFs. Even a "mistake" in approving a contract between a utility and a QF does not establish sufficient grounds to overcome this preemption. Moreover, in the instant case, there can have been no mistake because the energy payments that Lake Cogen asserts are due under the Contract are entirely consistent with the projected energy payments that were considered by the Commission, and indeed incorporated into the Commission's order approving the Contract, in 1991.

A. The Commission Is Preempted By Federal Law From Revisiting Its Approval Of, Or Denying Cost Recovery Of Amounts Paid Pursuant To, Previously Approved Cogeneration Contracts.

The Commission is preempted by PURPA from revisiting its approval of contracts between QFs and utilities that it has previously found to be consistent with avoided costs. The Commission is similarly preempted by PURPA from denying the recovery, by the utility from its ratepayers, of payments made to QFs pursuant to such previously approved contracts. See, e.g., Freehold Cogeneration Assocs., L.P. v. Board of Regulatory Comm'rs., 44 F.3d 1178, 1194 (3d Cir.), cert. denied, 116 S. Ct. 68 (1995) ("Freehold") ("once [a State Commission has] approved [a] power purchase agreement between [a utility and a QF] . . . any action or order by the [Commission] . . . to deny the passage

of th[e] rates [payable under that contract] to [the utility's] consumers . . . [is] preempted by federal law").[2]

The overriding goal of PURPA is "to encourage the development of cogeneration . . . facilities." FERC v. Mississippi, 456 U.S. 742, 750-51 (1982). Through PURPA, Congress compelled[3] electric utilities, such as FPC, to enter into long-term contracts to purchase energy from qualifying cogeneration facilities ("QFs"), such as Lake Cogen. See, e.g., 16 U.S.C. § 824a-3(a). Section 210(a) of PURPA, 16 U.S.C. 824a-3(a), requires the U.S. Federal Energy Regulatory Commission ("FERC") to prescribe "such rules as it determines necessary to encourage cogeneration"; PURPA also mandates that each state's public utility commission must implement FERC's rules and may be sued by FERC (or a QF) for any failure to do so. 16 U.S.C.

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[2] Preemption under the Supremacy Clause of the United States Constitution results under several circumstances: (a) where Congress, in enacting a statute, or a federal agency acting within the scope of its delegated authority, expresses an intent to preempt state law, (b) when there is a conflict between federal and state law, (c) where federal law is so comprehensive as to occupy the field of regulation leaving no room for state supplementation, or (d) where state law stands as an obstacle to the accomplishment and execution of the full objectives of Congress. See Louisiana Public Serv. Com. v. FCC, 476 U.S. 355, 368-69 (1986). Among other things, PURPA expressly preempts "State laws and regulations respecting the rates [charged by QFs]," as well as the application to QFs of state laws "respecting the financial or organizational regulation, of electric utilities." See 16 U.S.C. § 824a-3(e); 18 C.F.R. § 292.602(c)(1).

[3] The Commission should recall that FPC was not compelled to enter into the Lake Cogen-FPC Contract nor any of the other Negotiated Contracts. The Lake Cogen-FPC Contract and the other Negotiated Contracts provided pricing below FPC's full avoided costs, see 91 FPSC 7:71, and were the product of a competitive bidding process initiated by FPC, see 91 FPSC 7:60, in its efforts to address its immediate needs for generating capacity. See 91 FPSC 7:62-64.

§§ 824a-3(f)(1), 3(h)(2)(A), (B).

FERC's regulations specifically address the rates to be paid by utilities to QFs for energy generated by the QF. A QF is entitled to the full amount of the utility's so-called avoided cost calculated at the time the QF's contractual obligation is incurred, even if the rates are based on estimated future avoided costs and ultimately differ from avoided costs at the time of delivery. 18 C.F.R. §§ 292.304(b)(5), 292.304(d). See also American Paper Inst., Inc. v. American Electric Power Serv. Corp., 461 U.S. 402, 413-18 (1983) (rates set at full avoided costs are fair and reasonable to the electric utility's ratepayers). "The import of this section is to ensure that a . . . [QF] which has obtained the certainty of an arrangement is not deprived of the benefits of its commitment as a result of changed circumstances." See Small Power Production and Cogeneration Facilities; Regulations Implementing Section 210 of the Public Utility Regulatory Policies Act of 1978, 45 Fed. Reg. 12214, 12224 (Feb. 25, 1980) (the "FERC Guidelines").

The need to afford long-term certainty to QFs is quite powerful. FERC has decreed that a QF's contract must be honored even "if the avoided cost of energy at the time it is delivered [by the QF] is less than the price provided in the contract," thus requiring a utility "to pay a rate for purchases that would subsidize the QF at the expense of the utility's other ratepayers." See New York State Electric & Gas Corp., 71 FERC ¶ 61,027, at 61,116 (1995); FERC Guidelines, 45 Fed. Reg. at 12224 (PURPA was intended to provide for certainty with respect to a QF's return on its investment and not "minute-by-minute

evaluation[s] of costs which would be checked against rates established" in long term QF contracts). And, FERC has refused to permit the reconsideration of QF contracts even where the utility or state commission submits that a mistake was made in the initial pricing of the QF's energy. See, e.g., Jersey Central Power & Light Company, 73 FERC ¶ 61,092 (Oct. 17, 1995).[4]

These rules and policies have precise application to the matter at hand. The Commission approved this Contract in July 1991. In its approval order, the Commission properly found that the Contract formula for setting the rates payable by FPC thereunder was well within the avoided cost parameters of PURPA. See In Re: Petition for Approval of Contracts, 91 FPSC 7:67-70. Indeed, as support for its approval of the Contract, the Commission adopted FPC's evidentiary proffer that the projected stream of estimated contract costs would result in payments below FPC's projection of applicable avoided costs. See id. Thus, this Commission ultimately concluded that the Contract and its pricing terms met "all the requirements and rules governing qualifying facilities." See id. at 91 FPSC 7:70.

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[4] It is noteworthy that the Commission has raised the cost recovery question in the context of the parties' attempt to obtain approval of a consensual resolution of contract pricing issues through a partial buy-down of the Contract. FERC has actively and publicly encouraged such settlements. See, e.g., West Penn Power Co., 71 FERC ¶ 61,153, at 61,497 (rather than engaging in futile attempts to invalidate QF contracts, utilities and state commissions should pursue consensual buy-outs or buy-downs of these contracts). Indeed, FERC has determined that, in the exercise of its jurisdiction over wholesale rates, it "will permit the recovery . . . of a pro rata share of [such] buy-out or buy-down costs." See id. Accordingly, Lake Cogen submits that the Commission's denial of the pass through of the Contract's costs or its rejection of the proffered settlement would clearly be contrary to FERC's directives in this additional respect.

Once the Commission approved the Contract on these grounds, PURPA, along with FERC's regulations, precludes any effort to revisit the rates or FPC's cost recovery of payments made under the Contract. For example, in Freehold, the prices payable by a utility, Jersey Central Power & Light Company ("JCP&L") to a QF, Freehold Cogeneration Associates ("Freehold"), were dramatically and demonstrably in excess of the utility's avoided cost, in part because the state regulatory authority, the New Jersey Board of Regulatory Commissioners ("BRC"), had mistakenly approved rates above avoided cost and in part due to changed circumstances. The New Jersey BRC thus initiated hearings to consider whether to modify its prior approval of the relevant cogeneration contract or to reduce JCP&L's ability to recover the costs incurred under that contract from its ratepayers. The utility supported the BRC's action, asserting, in part, that a "regulatory out" clause in the contract would permit it to reduce payments to the QF to the extent that the BRC reduced the utility's recovery from its ratepayers.

The Third Circuit held that, despite the fact that contract payments turned out to be greater than JCP&L's avoided costs, and despite the fact that the New Jersey BRC apparently approved Freehold's contract on the basis of avoided cost projections that were already outdated and too high, as of the date the Freehold-JCP&L contract was approved, PURPA preempted the BRC from taking either of the actions it was considering. Having approved the contract as being consistent with PURPA, the BRC could not take any action to reconsider its approval of the contract or to deny the collection of the utility's costs thereunder from its

customers. Specifically, the Court held, in no uncertain terms, that "once the BRC approved the power purchase agreement between Freehold and JCP & L on the ground that the rates were consistent with avoided cost, just, reasonably, and prudentially incurred, any action or order by the BRC to reconsider its approval or to deny the passage of those rates to JCP & L's consumers under purported state authority was preempted by federal law." Freehold, 44 F.3d at 1194.[5]

Other courts have concurred with the Freehold analysis. In West Penn Power Co. v. Pennsylvania Pub. Util. Comm'n., 659 A.2d 1055 (Commw. Ct. 1995), the Court followed Freehold in determining whether the Pennsylvania state commission had any authority to review prior orders approving PURPA contracts. 659 A.2d 1055. The Court concluded: "Unless or until PURPA is amended or repealed, reestablishing [state] regulatory power over the area, it appears that the [state commission] cannot reexamine contracts for PURPA power." West Penn, 659 A.2d at 1066-67; accord Smith Cogeneration Management v. Corporation Comm'n & Pub. Serv. Co., 863 P.2d 1227, 1240-41 (Okla. 1993) ("[r]econsideration of long-term contracts with established estimated avoided costs" is preempted by PURPA); Independent Energy Producers Ass'n v. California Pub. Utils. Comm'n, 36 F.3d 848, 858-59 (9th Cir. 1994).

Applicable federal law requires the same result here. In

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[5] The Freehold Court further held that the "regulatory out" clause did not confer on the BRC any jurisdiction it would not otherwise have and did not deprive the QF of any of its protections under PURPA. 44 F.3d at 1194.

this case, the Florida PSC approved the Lake Cogen-FPC Contract on the grounds that the Contract was cost-effective and "meet[s] all the requirements and rules governing qualifying facilities. See 91 FPSC 7:69-70. Having thus approved the Contract, the Commission is "preempted by federal law" from taking "any action . . . to reconsider its approval or to deny the passage of" payments pursuant to the Contract to FPC's ratepayers. Moreover, for the Commission to declare, as a generic matter, that it may reconsider and potentially deny cost recovery under previously approved utility-QF contracts, would be very similar to the Oklahoma Corporation Commission rule declared invalid by the Oklahoma Supreme Court in Smith Cogeneration. In that case, the Oklahoma Supreme Court held that an Oklahoma Corporation Commission rule, purporting to require utilities and QFs to include in contracts a provision giving that commission the authority to review and modify the terms of utility-QF contracts throughout the life of such contracts, was preempted by PURPA.

In short, preemption here is mandated for two basic reasons. First, by denying rate recovery, this Commission would, in effect, be engaging in post-approval regulatory review of the reasonableness of the merits or the pricing, or both, of the Contract. PURPA expressly prohibits a state commission from engaging in such regulation of QFs. See 16 U.S.C. § 824a-3(e); H.R. Conf. Rep. 95-1250, U.S. Code & Admin. News 1978, pp. 7831-32 (1978). Any other result would deprive QFs of "certainty with regard to [the] return on [their] investment[s]." See New York State Electric & Gas Corp., 71 FERC ¶ 61,027, at 61,116 (quoting FERC Guidelines, 45 Fed. Reg. at 12,224); see also Freehold, 44

F.3d at 1190-94; Independent Energy Producers, 36 F.3d at 858-59; Smith Cogeneration, 863 P.2d at 1239-41.

Second, the so-called filed-rate doctrine forecloses any Commission attempt to impair FPC's right to cost recovery. Under PURPA, the wholesale rates charged by QFs are determined exclusively under federal law, including FERC's regulations. See Connecticut Light and Power Co., 70 FERC ¶ 61,012, at 61,027 (1995) ("For QFs, jurisdiction over rates for sales at wholesale is vested in" FERC). Numerous Supreme Court cases hold that "a state utility commission setting retail prices must allow, as reasonable operating expenses, costs incurred [by a utility] as a result of paying a FERC-determined wholesale price." See Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953, 965 (1986); see also Mississippi Power & Light Co. v. Mississippi, 487 U.S. 354, 371-72 (1988) ("States may not bar regulated utilities from passing through to retail consumers FERC-mandated wholesale rates"); Narragansett Elec. Co. v. Burke, 119 R.I. 559, 381 A.2d 1358 (1977), cert. denied, 435 U.S. 972 (1978) (federally approved rates must be honored by state regulatory agencies in setting the purchasing utility's retail rate). Several PURPA cases confirm that the Commission may not use its typical regulatory powers with respect to the pass-through of federally determined -- and protected -- pricing under previously-approved PURPA contracts. See Freehold, 44 F.3d at 1190-94; West Penn, 659 A.2d at 1065-67.

Finally, it would be particularly troublesome for the Commission to effectively attempt to "overrule" or supplant the determination by a State court as to the rates payable by FPL

under the Contract. It is State law that determines the "specific parameters of individual QF power purchase agreements." See West Penn, 71 FERC ¶ 61,153, at 61,495. Applying FERC's avoided cost rule and basic contract law, State courts often are the ultimate arbiters of the proper contract rate, including the appropriate avoided cost standard, under PURPA contracts. See, e.g., Armco Advanced Materials Corp. v. Pennsylvania Pub. Util. Comm'n., 664 A.2d 630 (Pa. Commw. Ct. 1995). Even if the Commission disagrees with a ruling by a Florida court as to the Contract, the Commission is bound by any such interpretation of the pricing formula, and it must allow full recovery of the contract costs incurred by FPC under that formula. See Freehold, 44 F.3d at 1190-94; see also Wright v. Florida Unemployment Appeals Comm'n, 512 So. 2d 333, 335 (Fla. 3rd DCA 1987, concurring opinion of Judge D.S. Pearson) (relevant court decisions are binding and controlling on administrative agencies).

B. Mistake Is Not Sufficient Grounds to Overcome Federal Preemption.

Neither "changed circumstances" nor a purported "mistake" in connection with a state commission's calculation of avoided costs can change the applicability of federal preemption in these circumstances. See, e.g., West Penn, 659 A.2d at 1065 (allegations of serious mistake did not justify state commission's reconsideration of approval of power purchase agreement). This is a vital point in light of the fact that the Commission now is viewing analyses of Lake Cogen's prices that rely upon circumstances that differ from those upon which the

initial avoided cost projections were based – i.e., FPC's new avoided cost model takes into account post-approval declines in energy prices, improved nuclear plant performance, etc. Under federal law, such matters simply cannot be considered by the Commission at this time. See, e.g., Freehold, 44 F.3d at 1190-94; Smith Cogeneration, 863 P.2d at 1239-41.

Mistake is not sufficient grounds to overcome the federal preemption of state utility commissions' authority with respect to payments made under previously approved utility-QF contracts. In Freehold, the New Jersey BRC effectively suggested that it had made a mistake in approving the Freehold-JCP&L contract based on incorrect avoided cost assumptions, i.e., avoided cost values that, due to a grandfathering process, were outdated and too high at the time the contract was approved. In its Petition for Rehearing to the Third Circuit, the BRC argued as follows:

> Having approved a PPA [Power Purchase Agreement] rate in excess of avoided cost, either **as a result of error** or based on what it then-believed was purported state authority, which it is now clear it does not have, the Board is not preempted by anything in PURPA from reconsidering its 1992 decision in accordance with its authority under [New Jersey statutes] to at any time order a rehearing and extend, revoke and modify an order made by it.

Petition of Defendant-Appellee Board of Regulatory Commissioners of the State of New Jersey for Rehearing with Suggestion for Rehearing In Banc, filed in Freehold Cogeneration Assocs. v. Board of Regulatory Comm'rs and Jersey Central Power & Light Co. (January 23, 1995) (emphasis supplied). (A copy of the relevant portion of this Petition is attached hereto as Appendix A.)

The U.S. Third Circuit Court of Appeals rejected this argument and held that "once the BRC approved the power purchase agreement between Freehold and JCP & L on the ground that the

rates were consistent with avoided cost, just, reasonably, and prudentially incurred, any action or order by the BRC to reconsider its approval or to deny the passage of those rates to JCP & L's consumers under purported state authority was preempted by federal law." Freehold, 44 F.3d 1194.

On a related note, as a matter of state law, the Pennsylvania Commonwealth Court held that the Pennsylvania Public Utilities Commission could not be found to have abused its discretion, where it refused to grant reconsideration of its order approving a cogeneration contract, even though the utility alleged that a mistake, even one that would result in serious adverse consequences to the utility's ratepayers, had occurred in the PUC's approval of the cogeneration contracts. West Penn, 659 A.2d at 1065. Relating the alleged abuse of discretion to federal preemption pursuant to PURPA, the Pennsylvania Court went on to hold as follows:

> [W]e concur that Section 210 of PURPA preempts the PUC from reconsidering its prior approval of the EEPAs [electric energy purchase agreements] between West Penn and the QFs or to change the rates established for the avoided costs at the time of the agreements. Unless or until PURPA is amended or repealed, reestablishing regulatory power over the area, it appears that the PUC cannot reexamine contracts for PURPA power. Because such an order would be preempted by federal law, the PUC did not abuse its discretion in refusing to rescind its prior orders as requested in West Penn's complaint.

Id. at 1066.

Thus, "mistake" does not establish sufficient grounds to overcome the federal preemption of state utility commissions' actions directed either at revisiting approval of contracts

between utilities and QFs or at denying cost recovery by the utilities of payments made pursuant to such contracts.

C. Even If Mistake Were Sufficient to Create Grounds To Revisit Contract Approval, There Was No Mistake In This Case.

As Lake Cogen pointed out in its brief in FPSC Docket No. 940771-EQ, even under what FPC, and apparently, some members of the Commission Staff, envision as the worst possible outcome of the lawsuit -- i.e., the case in which Lake Cogen would prevail in the lawsuit and FPC would be ordered to pay Lake Cogen the Firm Energy Price for all energy delivered to FPC -- there are no grounds to assert that a mistake has occurred. In that event, all that would have happened is that the Circuit Court would have held that FPC must make payments to Lake Cogen in exactly the manner that FPC projected to the Commission such payments would be made, i.e., "the firm energy price all the time." In that case, the Court-ordered energy payments would exactly track the projected payments contemplated by the Commission's Order No. 24734 approving the Lake Cogen-FPC Contract (and the other Negotiated Contracts), and in fact included as part of that Order, with the only differences being for market fluctuations in the price of coal and for the Performance Adjustment Factor specified within the Contract, to the extent applicable.

II. THE COMMISSION IS PRECLUDED BY THE DOCTRINE OF ADMINISTRATIVE FINALITY FROM REVISITING ITS PRIOR APPROVAL, FOR COST RECOVERY PURPOSES, OF THE LAKE COGEN-FPC CONTRACT.

In its Order No. 25668, explicating the meaning and workings of its rules governing the relationships between QFs and

utilities under negotiated power sales contracts, the Commission wrote the following:

> The doctrine of administrative finality is one of fairness. It is based on the premise that the parties, as well as the public, may rely on Commission decisions. We, therefore, find that a utility and a QF should be able to rely on the finality of a Commission ruling approving cost recovery under a negotiated contract. Once an order approving a negotiated contract becomes final by operation of law, we may not at a later date deny cost recovery to the utility, absent a showing that our approval was induced through perjury, fraud, collusion, deceit, mistake, inadvertence, or the intentional withholding of key information.

In Re: Implementation of Rules 25-17.080 Through 25-17.091, F.A.C., Regarding Cogeneration and Small Power Production, 92 FPSC 2:24, 38.

In the same Order, the Commission also wrote that "negotiated contracts should be treated in the same manner as standard offer contracts for cost recovery purposes." Id., 92 FPSC 2:36. In Florida Power & Light Co. v. Beard, 626 So. 2d 660 (Fla. 1993), the Court upheld the Commission's prohibition, by rule, of "regulatory out" clauses from standard offer contracts on the grounds that such clauses "create a mistaken perception that revenues under a standard offer are not reliable," id. at 662 (quoting from FPSC Order No. 24989 at 70-71), and that "utilities and QFs should be able to rely on the finality of the approval of cost recovery under standard offer contracts without fear of modification." Id.

If the Commission were to declare, in this case, that it may undertake a proceeding to revisit its approval of the Lake Cogen-FPC Contract, with one possible outcome being the denial of cost recovery to FPC of amounts paid under the Contract, it would have

effectively abrogated and negated its prior pronouncements as to utilities' and QFs' ability to rely on the Commission's orders approving contracts between them. The Commission would also have acted contrary to the Supreme Court's holding in Beard.

III. THE COMMISSION'S DENIAL OF THE LAKE COGEN-FPC SETTLEMENT AGREEMENT, WHERE THE COMMISSION HAS ALREADY APPROVED A SUBSTANTIALLY IDENTICAL SETTLEMENT AGREEMENT BETWEEN PASCO COGEN AND FPC, WOULD VIOLATE THE FLORIDA ADMINISTRATIVE PROCEDURE ACT AND THE EQUAL PROTECTION GUARANTEES OF THE FLORIDA AND UNITED STATES CONSTITUTIONS.

Under Florida administrative law, "persons have the right to locate precedent and have it apply, and the right to know the factual basis and policy reasons for agency action." Amos v. Dep't of Health & Rehab. Services, 444 So. 2d 43, 47 (Fla. 1st DCA 1983) (agency action denying AFDC benefits to an applicant reversed where, five months earlier, the agency had granted such benefits to an applicant under similar circumstances); see also State ex rel. Department of General Services v. Willis, 344 So. 2d 580 (Fla. 1st DCA 1977). "Inconsistent results based upon similar facts, without a reasonable explanation, violate Section 120.68(12)(b), Florida Statutes, as well as the equal protection guarantees of both the Florida and United States Constitutions." Amos, 444 So. 2d at 47, citing North Miami General Hospital, Inc. v. Office of Community Medical Facilities, 355 So. 2d 1272, 1278 (Fla. 1st DCA 1978) (agency's denial of approval, for cost reimbursement purposes pursuant to Social Security Act, of medical equipment purchase by hospital was reversed where, inter alia, while North Miami General's application was pending, agency had granted approval to another applicant under similar

circumstances); see also St. Johns North Utility Corp. v. Florida Public Service Comm'n, 549 So. 2d 1066, 1069 (Fla. 1st DCA 1989) (dicta recognizing the general principle that "the agency bears the burden of providing a reasonable explanation for inconsistent results based upon similar facts. Failure to do so violates section 120.68(12)(b) and the equal protection guarantees of the Florida and federal constitutions.")

This standard, that agency action must generally produce consistent results based on similar facts, is similar to the "arbitrary and capricious" standard of review that is also applied to agency action. See University Community Hosp. v. Dep't. of Health & Rehab. Services, 472 So. 2d 756, 757-58 (Fla. 2nd DCA 1985) (The appellate court is "to affirm final agency action 'unless that decision is found to be arbitrary, capricious, or not in compliance with' [the Administrative Procedure Act]." (citations omitted) "Persons and entities affected by administrative proceedings must be able to rely on precedents born of consistent application of policy to facts.")[6]; see also Agrico Chemical Co. v. Department of Environmental Regulation, 365 So. 2d 759, 763 (Fla. 1st DCA 1979) (arbitrary and capricious standard applied in appeal of agency rule).

This standard is also similar to the principle of "administrative stare decisis" enunciated by the Fourth District

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[6] In fact, HRS's arbitrary and capricious action in University Community Hospital was found to constitute a gross abuse of agency discretion giving rise to an award of attorneys' fees and costs to the aggrieved hospital pursuant to Section 120.57(1)(b)10, Florida Statutes (1995). University Community Hospital v. Dep't of Health & Rehab. Services, 492 So.2d 1339 (Fla. 2nd DCA 1985); University Community Hospital v. Dep't of Health & Rehab. Services, 493 So.2d 2 (Fla. 2nd DCA 1986).

Court of Appeal in Gessler v. Dep't of Business & Professional Regulation, 627 So. 2d 501, 503-504 (Fla. 4th DCA 1993). Gessler involved the agency's ongoing failure to index its orders so that substantially affected persons would have the opportunity to "examine agency precedent and . . . to know the factual basis and policy reasons for agency action." Gessler, 627 So. 2d 503. The Fourth DCA went on to state the following:

> The concept of stare decisis, by treating like cases alike and following decisions rendered previously involving similar circumstances, is a core principle of our system of justice. . . . While it is apparent that agencies, with their significant policy-making roles, may not be bound to follow prior decisions to the extent that the courts are bound by precedent, it is nevertheless apparent the legislature intends there be a principle of administrative stare decisis in Florida.

Gessler, 627 So. 2d 504.

Here, Lake Cogen and FPC have come before the Commission seeking approval of a settlement agreement that is substantially identical to the one between Pasco Cogen, Ltd. and FPC that the Commission previously approved in Docket No. 961407-EQ. Here, Lake Cogen and FPC are entitled to have the same analysis applied to their settlement and the same result as that reached by the Commission in Docket No. 961407-EQ, based on the near-total identity of the facts adduced in these two companion dockets.

Section 120.68(12)(b), Florida Statutes, provides for remand where agency action is "inconsistent with . . . prior agency practice, if deviation therefrom is not explained by the agency." Lake Cogen submits that the Commission's denial of the same treatment as that afforded the Pasco Cogen-FPC settlement would

be plainly inconsistent with the Commission's prior practice, and Lake Cogen further submits that no reasonable explanation for a deviation from the Commission's decision on the Pasco Cogen-FPC settlement is possible. As noted above, the energy pricing terms of both settlement agreements are identical, the modified capacity payments are identical for the years 1996 through 2008 (the termination year of the amended Pasco Cogen-FPC Contract), and the initial settlement payments are identical ($5.5 million to Lake Cogen and $5.5 million to Pasco Cogen). The only noticeable differences are (1) a one-year difference in the buyout period; (2) the buyout payments are different, corresponding to the different buyout periods; and (3) greater curtailment benefits provided to FPC and its ratepayers by the Lake-FPC Settlement Agreement than by the Pasco-FPC Settlement. See FPC's Petition and attachments, FPSC Document No. 12578, filed in FPSC Docket No. 961407-EQ, November 25, 1996; FPC's Petition and attachments, FPSC Document No. 13260, filed in FPSC Docket No. 961477-EQ, December 12, 1996; and FPSC Order No. 97-0523-FOF-EQ.

The difference in the estimated net present value of savings to FPC and its ratepayers between the two settlements is minimal, $27.5 million under the Pasco Cogen settlement and $26.7 million under the Lake Cogen-FPC settlement. In fact, given that the Lake Cogen-FPC Settlement provides significantly greater curtailment benefits (specifically, 28.5 percent more curtailment benefits, 18 MW under the Lake Cogen-FPC Settlement vs. 14 MW under the Pasco Cogen-FPC Settlement), and given that the shorter buyout period under the Lake Cogen-FPC settlement reduces the

concerns regarding assertedly speculative benefits of the buyout raised by the Commission Staff, Lake Cogen submits that, if anything, the Lake Cogen-FPC Settlement Agreement is even more favorable to FPC and its ratepayers than the Pasco-FPC settlement.

As the courts in Amos and North Miami General stated, "inconsistent results based upon similar facts, without a reasonable explanation, violate Section 120.68(12)(b), Florida Statutes, as well as the equal protection guarantees of both the Florida and United States Constitutions." Lake Cogen and FPC are entitled to the same result reached in the Pasco-FPC settlement docket, both under Florida's Administrative Procedure Act and under the Florida and U.S. Constitutions.

CONCLUSION

WHEREFORE, based on the foregoing, the Commission should recognize that it is preempted by federal law from revisiting cost recovery under the already-approved Contract between Lake Cogen and FPC, regardless of the interpretation of that Contract that may be applied by the Lake County Circuit Court. Commission action attempting to interpret the Lake Cogen-FPC Contract would be inconsistent with the doctrine of administrative finality, as well as inconsistent with the Commission's own prior pronouncements regarding its role with respect to approved contracts between QFs and utilities. Finally, for the Commission to refuse to approve the Lake Cogen-FPC Settlement, where it recently approved the nearly identical settlement between Pasco Cogen and FPC, would violate the Florida Administrative Procedure

Act and the equal protection guarantees of both the Florida and United States Constitutions. Accordingly, the Commission should not disturb its prior approval of the Settlement Agreement between Lake Cogen and Florida Power Corporation.

Respectfully submitted this 29th day of July, 1997.

LAKE COGEN, LTD.,
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APPENDIX A

EXCERPT FROM

PETITION AND APPENDIX OF DEFENDANT-APPELLEE BOARD OF REGULATORY COMMISSIONERS OF THE STATE OF NEW JERSEY FOR REHEARING, WITH SUGGESTION FOR REHEARING IN BANC

FILED IN

FREEHOLD COGENERATION ASSOCIATES v. BOARD OF REGULATORY COMMISSIONERS OF THE STATE OF NEW JERSEY AND JERSEY CENTRAL POWER & LIGHT COMPANY,

IN THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT, DOCKET NO. 94-5168

PETITION FOR REHEARING WITH SUGGESTION FOR REHEARING IN BANC

Pursuant to Fed. R. App. P. 40, the Defendant-Appellee, New Jersey Board of Public Utilities[1] ("Board"), hereby petitions for a rehearing of this appeal and respectfully suggests that such hearing should be in banc. Fed. R. App. P. 35. Specifically, the Board respectfully seeks reconsideration of a decision (attached hereto filed January 9, 1995 (the Honorable Max Rosenn, Senior Circuit Judge, the Honorable Walter K. Stapleton and the Honorable William J. Hutchinson, Circuit Judges). The Circuit Court's decision reverses the Memorandum and Order of District Judge Mary Little Parell denying the summary judgment motion of Plaintiff-Appellant, Freehold Cogeneration Associates, L.P. ("Freehold"), and granting the Defendants'-Appellees' motions to dismiss.

As counsel of record for the Defendant-Appellee, the New Jersey Board of Public Utilities, I express a belief, based upon a reasoned and studied professional judgment, that this case involves a question of exceptional importance, to wit, the Circuit Court's decision that the Board is preempted under Section 210(e) of the Public Utilities Regulatory Policies Act (PURPA), 16 U.S.C. §796 and §824a-3 et seq.[2], from initiating a proceeding to consider whether it could and should reconsider a prior Order approving a power purchase agreement (PPA) and allowing the pass-through of those costs to customers, notwithstanding the fact that the Board-approved rate

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[1] By Reorganization Plan No. 001-1994, the New Jersey Board of Regulatory Commissioners was redesignated the New Jersey Board of Public Utilities, effective July 4, 1994. 26 N.J.R. 2171 (June 6, 1994).

[2] 16 U.S.C. §824a-3 et seq. is commonly referred to as Section 210 of PURPA.

exceeds the maximum rate authorized by Section 210(b) of PURPA and that there may have been negotiated provisions in the PPA beyond the requirements of PURPA, is incorrect and in conflict with the Congressional mandate under PURPA that rates for the purchase of power by an electric utility from a qualifying facility (QF) be "just and reasonable to the consumers of the electric utility" and shall not exceed the avoided cost, i.e., the incremental cost to the electric utility of alternative energy. 16 U.S.C. §824a-3(b), 18 C.F.R. §§292.303 and 292.304.

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PRELIMINARY STATEMENT

Defendant-Appellee, New Jersey Board of Public Utilities is taking the extraordinary step of seeking reconsideration in banc of the Circuit Court's decision because of the significance of this issue both as a matter of law and as a matter of practical effect on the State of New Jersey, its electric utilities and its ratepayers. As will be argued herein, the Circuit Court's conclusory finding that the Board is preempted under Section 210(e) of PURPA from conducting a fact finding proceeding to consider whether it can and should reconsider its prior Order approving and allowing rate recovery for a PPA where the Board-approved rate exceeds the maximum PURPA rate, constitutes an incorrect reading of PURPA, affording undue protection to QFs contrary to the express requirements of Section 210(b) of PURPA and to the detriment of consumers. The Circuit Court's decision seriously impairs the ability of state regulatory commissions to discharge their regulatory duty to ensure that utilities provide electric service to

ARGUMENT

THE BOARD IS NOT PREEMPTED BY PURPA FROM HOLDING A PROCEEDING TO CONSIDER THE QUESTION OF WHETHER IT CAN AND SHOULD MODIFY A PRIOR ORDER APPROVING A PPA TO THE EXTENT THE APPROVED RATE EXCEEDS THE MAXIMUM PURPA RATE OR TO THE EXTENT THE PARTIES MAY HAVE AGREED TO TERMS AND CONDITIONS BEYOND THOSE PROTECTED BY PURPA

The Circuit Court concluded in this case that once the Board had approved the instant PPA between Freehold and JCP&L, "any action or order by the [Board] to reconsider its approval or deny the passage of those rates to JCP&L's consumers under purported state authority was preempted under federal law." (Opinion, *14). In reaching this sweeping conclusion, the Court ignored the critical fact that the PPA entered into and approved by the Board in 1992 provided for a rate which was in excess of the maximum rate authorized by PURPA. Section 210(b) of PURPA sets full avoided cost as the maximum rate that FERC may prescribe. American Paper Inst. v. American Electric Power Service Corp., 461 U.S. 402, 413 (1983). The FERC rules provide that if a QF sells electric power pursuant to a legally enforceable obligation over a specified term, the rates for such purchases shall, at the option of the QF, be based on the avoided costs either at the time of delivery, or calculated "at the time the obligation is incurred." 18 C.F.R. §292.304(d). It has been held that where, as in this case, a PPA provides that it will not become effective until approved by the state regulatory commission, the legally enforceable obligation is deemed to have been incurred at the time state regulatory approval is obtained. In re Vicon Recovery Systems, Inc., 572 A. 2d 1344, 1360 (Vt. 1990).

The Board argued to the Circuit Court that, while it was in the process of affording the parties an opportunity to be fully heard

and therefore had not yet ruled on the issue of whether it was preempted under PURPA from modifying its 1992 Order, given the particular facts of this PPA, there were unresolved issues of fact and law as to whether the Board was preempted from reconsidering its 1992 Order. The Board respectfully contends that having in 1992 approved a PPA, with a rate in excess of the Section 210(b) PURPA maximum rate, either as a result of error or based upon what was then believed to be purported state authority[6], the Board is not preempted by Section 210(e) of PURPA from reconsidering its approval to the extent the approved rate exceeds the maximum PURPA rate.[7] To the contrary, a recent decision by FERC, issued only two days after the decision of the Circuit Court, In re Connecticut Light and Power Company, supra, concludes that state commissions have no authority under federal law to prescribe rates for sales by QFs to electric utilities at rates that exceed the avoided cost cap in PURPA. (Id. at 15). FERC notes in its opinion that for states to mandate rates above avoided costs runs

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[6] In its 1980 preamble to the FERC rules, FERC appears to have suggested that states could exercise state authority independent of PURPA to impose a rate exceeding avoided cost. FERC Stats. & Regs, Regulations Preambles 1977-1981 at 30,875. However, in a recent decision, FERC specifically disavows this view and concludes that states have no authority to impose a rate exceeding avoided cost. In re Connecticut Power and Light Co., supra.

[7] The Division of the Ratepayer Advocate argued to this Court that the Board's approval of the 1989 rate in 1992 was ultra vires, but the Court refused to entertain this argument, on the grounds that it had not raised this issue to the District Court, citing Patterson v. Cuyler, 729 F.2d 925 (3rd Cir. 1984). (Opinion *5, n.3). This was an issue that the Ratepayer Advocate was pursuing in the state proceeding before the Board. The Board further notes that although the issue of whether the Board's approval was ultra vires may not have been presented to the District Court as such, the issue that the approved rate exceeded the PURPA maximum rate was indeed raised by the Defendants-Appellees. In any event, the District Court never reached the merits of the case, dismissing Freehold's complaint on jurisdictional grounds.

counter to Section 210(b) of PURPA as well as Congress' and FERC's current policies "which strongly favor competition among all bulk power suppliers." (Id. at 15-16). While FERC indicates that it will apply its decision prospectively (Id. at 17), nothing in the decision suggests that under federal law, a state, on its own motion, cannot reconsider a prior decision approving a PPA rate and rate passthrough in excess of the PURPA maximum.

The Circuit Court concluded that PURPA bars reconsideration of the approval of the PPA "absent some basis in the law of contracts for setting aside the PPA." (Opinion, *12). The Circuit Court also stated that no claim of fraud or mutual mistake of fact is alleged in the negotiation and execution of the PPA. (Opinion, *10). However, in seemingly limiting reconsideration to issues of contract law as it pertains to the contracting parties themselves, the Court overlooks the Board's regulatory role. The PPA at issues is not simply a private contract between two parties, one of whom now wishes to be relieved of its obligations. This is a contract with a public utility whose rates are regulated in the public interest and whose rates are required by law to be just and reasonable. PURPA itself makes it abundantly clear that rates for the purchase of power by an electric utility from a QF must be "just and reasonable to the consumers of the electric utility" and may not exceed the incremental cost to the electric utility of alternative energy. 16 U.S.C. §824a-3(b). Congress has further stated that the provisions of PURPA were "not intended to require the ratepayers of a utility to subsidize cogenerators." H.R. Conf. Rep. No. 95-1570 p.98 (1978), reprinted in 1978 U.S.C.C.A.N. 7659, 7832. Although Freehold would clearly want it otherwise, the fact remains

that it was never the express intent of Congress or FERC that a utility's ratepayers would be compelled to pay rates for power purchases from a QF in excess of the utility's avoided costs. Clearly, the FERC rules place implementation of its avoided cost scheme in the hands of the state regulatory authority. 18 C.F.R. §292.401. Pursuant to that authority, the Board has required that all PPAs between QFs and New Jersey electric utilities must be approved by the Board to assure that the rates in such agreements are just and reasonable to the utility and its customers. Having approved a PPA rate in excess of avoided cost, either as a result of error or based on what it then-believed was purported state authority, which it is now clear it does not have, the Board is not preempted by anything in PURPA from reconsidering its 1992 decision in accordance with its authority under N.J.S.A. 48:2-40 to "at any time order a rehearing and extend, revoke and modify an order made by it." Indeed, while the basic premise of preemption is to render unenforceable state laws which are inconsistent with federal law (Opinion, *10), consideration by the Board of whether in 1992 it had approved rates in excess of the utility's avoided costs is fully consistent, and not inconsistent, with Section 210(b) of PURPA.

Such reconsideration by the Board was not intended to be, nor does it constitute, impermissible "utility-type" regulation under Section 210(e) of PURPA. PURPA and the FERC regulations provide that QFs are exempt from state laws regulating electric utility rates and financial organization. 18 C.F.R. §292.602(c). Legislative history shows that Congress wanted to ensure that the rates for cogeneration would not be subject to the same type of scrutiny as are typical state

CERTIFICATE OF SERVICE
DOCKET NO. 961477-EQ

I HEREBY CERTIFY that a true and correct copy of the foregoing has been served by hand delivery (*) or by United States Mail, postage prepaid, on the following individuals this 29th day of July, 1997:

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