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Compensation for Transmission Facilities Owned by Municipal Utilities

Background, Methods
and Principles

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Why this topic? Why now?

- Transmission Customers are entitled to compensation for networked transmission facilities they own.
 - Orders 888 and 890 (OATT §30.9 credits)
 - RTO Tariff provisions for “traditional” (*i.e.*, direct) recovery of owner’s costs
- Yet, some municipal utilities that own transmission still haven’t taken action to secure the compensation to which they are entitled.



- Reasons some customers haven't sought compensation
 - Establishing book cost of old equipment
 - Complying with FERC accounting requirements
 - Exposure to obligations accompanying cost recovery (*e.g.*, burdens of RTO involvement, duty to construct, etc.)
- Factors that have put a higher priority on obtaining compensation
 - NERC compliance costs
 - Mitigation of transmission service cost increases
 - Risk and cost-sharing business models

What Facilities are Entitled to Compensation?

- Facilities must be “transmission”
 - FERC Seven-factor Test
 - Developed in Order 888 for a different purpose
 - Applied as a threshold for distinguishing T from D
 - Flexible, functional analysis
 - RTO Tariff definitions of “Transmission”
 - Example: SPP Attachment AI



- Transmission facilities must be “integrated” with the grid.
- Fact-driven analysis, but:
 - **Presumption that transmission facilities are integrated**
 - FERC’s “any degree of integration” standard
 - Presumption extended to new customer-owned facilities in Order 890
 - ***Mansfield* Five-Factor Test for non-integration**
 - Only one of the Mansfield elements needs to be satisfied for “integration” finding
 - **Potential future uses and comparability with “host zone” facilities also are considerations.**

- Cases on rolled-in cost recovery versus direct assignment of Transmission Provider facilities are useful in addressing entitlement to compensation for Transmission Customer-owned facilities.
 - Compensation for customer-owned facilities “rolls in” the costs to the zone.
 - Denial of compensation “directly assigns” a facility’s cost to the customer.
 - FERC’s rolled-in pricing policy favors compensation for integrated facilities owned by transmission customers.

Compensation Approaches



- Goal is recovery of “Annual Revenue Requirement”
- Rate format
 - **Stated rate**
 - Requires FERC filing to change (affects regulated rates)
 - May over or under-recover actual cost in any given year
 - **Annually updating formula**
 - Based on FERC Accounts
 - Can be historical or forward-looking with true-up
 - **Historical also can over or under recover costs**
 - **Not an issue with forward-looking/true-up**
 - Formula rates must include protocols for customer review and challenge of ATRR

Calculating the Annual Revenue Requirement

- Rate base/rate of return (non-levelized) method
 - Replicating original cost can be a challenge.
 - In some settings, Municipals may be allowed to incorporate return on equity of interconnected transmission owner.
- Levelized fixed charge rate (FCR) applied to original cost
 - Issue of replicating original cost remains
 - FCR incorporates return, depreciation, O&M, etc.
 - Same charge over life of facility
 - Not a preferred approach; limited usefulness
 - Has been allowed for single-facility revenue requirement



- “Debt Service” method
 - O&M, A&G, etc. are recovered through formula
 - Fixed cost recovery is based on annual cost of debt used to finance integrated facilities plus a “Margin Requirement” (specified multiple of annual debt service)
 - Capital cost recovery is through the portion of debt service expense attributable to pay-down of principal
 - Fairly common method in SPP, MISO; recently approved for a new joint municipal transmission owner in PJM

Conclusion

- Mechanisms are in place for transmission-owning municipal utilities to be compensated for their integrated transmission facilities.
- FERC has not been unreceptive to compensation requests (encourages diversity of transmission ownership).
- Factors that have been a deterrent in the past can be overcome.

Appendix 1:

FERC Seven-Factor Test for Distinguishing “Transmission” from “Local Distribution”



Indicators of local distribution:

- (1) Local distribution facilities are normally in close proximity to retail customers;
- (2) Local distribution facilities are primarily radial in character;
- (3) Power flows into local distribution systems, and rarely, if ever, flows out;
- (4) When power enters a local distribution system, it is not reconsigned or transported onto some other market;
- (5) Power entering a local distribution system is consumed in a comparatively restricted geographic area;
- (6) Meters are based at the transmission/local distribution interface to measure flow into the local distribution system; and
- (7) Local distribution systems will be of reduced voltage.

Appendix 2:

Mansfield Five-Factor Test for “Integration”

Indicators of integration:

1. Whether facilities are radial or loop back into the system;
2. Whether energy flows only in one direction (from the transmission system to the customer) over the facilities, or in both directions;
3. Whether the transmission provider is able to provide transmission service to itself or other transmission customers over the facilities;
4. Whether the facilities provide benefits to the transmission grid in terms of capability or reliability, and whether the facilities can be relied on for coordinated operation of the grid; and
5. Whether an outage on the facilities would affect the transmission system.



Appendix 3: A Sampling of Pertinent FERC Decisions*

- *Niagara Mohawk Power Corp.*, 42 FERC ¶ 61,143 (1988) (FERC favors rolled-in cost allocation for transmission except in “special circumstances”).
- *Northeast Texas Electric Coop., Inc.*, 108 FERC ¶ 61,084 (2004), *reh’g denied*, 111 FERC ¶ 61,189 (2005) (applies presumption against direct assignment of costs of transmission facilities that provide transmission service to the transmission provider or other transmission customers; finds that lines provide backup provide a system-wide benefit).

* Not intended to be comprehensive. Case squibs are not meant to be definitive and do not substitute for the full text of decisions and consideration of the factual context in which cases arose.



- *Preventing Undue Discrimination and Preference in Transmission Service*, Order No. 890, 118 FERC ¶ 61,119, *order on reh'g*, Order No. 890-A, 121 FERC ¶ 61,297 (2007), *order on reh'g*, Order No. 890-B, 123 FERC ¶ 61,299 (2008), *order on reh'g*, Order No. 890-C, 126 FERC ¶ 61,228, *order on clarification*, Order No. 890-D, 129 FERC ¶ 61,126 (2009) (revised §30.9 of the pro forma OATT to make a network customer eligible for credits if it demonstrates that its facilities are integrated with the operations of the transmission provider's facilities, provided that integration will be presumed for new customer-owned facilities that, if owned by the transmission provider, would be eligible for inclusion in the transmission provider's annual transmission revenue requirement).
- *Mansfield Municipal Electric Dept. v. New England Power Co.*, 97 FERC ¶61,134 (2001), *reh'g denied*, 98 FERC ¶ 61,115 (2002) (five-factor integration test).
- *City of Anaheim*, 113 FERC ¶ 61,091 (2005) (*Mansfield* test determines whether special circumstances exist such that a facility is not a network facility. A negative showing as to all five *Mansfield* factors indicates that a facility is not integrated with the transmission network and that its costs should not be rolled into transmission rates; in contrast, it is not necessary that a facility make a positive showing with regard to all five *Mansfield* factors to be a network facility).



- *Duke Energy Carolinas, LLC*, 168 FERC ¶ 61,190 (2019) (“pursuant to the ‘any degree of integration’ test, a radial facility need only meet one of the five Mansfield criteria to be considered integrated into a transmission provider’s transmission system”).
- *El Paso Electric Co.*, 10 FERC ¶ 63,008 (1980), *aff’d in relevant part*, 14 FERC ¶61,082 (1981), and *Public Service Co. of Colorado*, 62 FERC ¶61,031 (1993) (cited in *Duke Energy Carolinas, LLC* for the proposition that “in determining whether a transmission line is part of an integrated system, potential future conditions as well as present circumstances must be evaluated.” *El Paso* itself relied on *Minnesota Power & Light Co.*, 3 FERC ¶ 61,045 (1978) for the principle that, in determining whether a transmission line is part of an integrated system, potential future conditions as well as current circumstances must be evaluated.).
- *Public Service Co. of Colorado*, 62 FERC ¶ 61,031 (1993) (cited in *Duke Energy Carolinas, LLC* for the proposition that rolled-in pricing is required if evidence shows the line in question would eventually benefit future customers other than the initial user of the line).



- *Southern Company Services, Inc.*, 116 FERC ¶ 61,247 (2006), *order on reh'g*, 119 FERC ¶ 61,023 (2007) (a showing of integration requires more than simply proof that the direct assignment of a transmission line to a wholesale customer is not comparable to how the transmission provider treats radial lines serving its retail customers; the solution in such instances, FERC said, is to remove the transmission provider's non-integrated lines from the rolled-in rate rather than to roll in other non-integrated lines). *Southern Company Services* has been narrowly construed. See, e.g., *Southwest Power Pool, Inc.*, 121 FERC ¶ 61,196 (2007)).
- *Buckeye Power v. American Transmission Systems, Inc.*, 148 FERC ¶ 61,174 (2014) (rolled-in cost allocation required for integrated lower-voltage facilities even though customers use lower-voltage and higher-voltage facilities differently).
- *AMP Transmission LLC*, 166 FERC ¶ 61,216 (2019) (approves use of debt service method in PJM and addresses issues related to Margin Requirement determination).
- *Southwest Power Pool, Inc.*, 147 FERC ¶ 61,003 (2014) (FERC evaluates level of Margin Requirement on a case-by-case basis).



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