



WHOLESALE TRANSMISSION RATES: IMPACT OF EMERGING ISSUES

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**Jason T. Gray
202.467-6370
jtg@dwgp.com
www.dwgp.com**

DWGP

DUNGAN WEINBERG GENZER BEMBRIDGE

RETURN ON EQUITY DEVELOPMENTS

1. Inquiry into the Combined Effect of FERC's Income Tax Allowance Policy and the DCF Methodology
2. Anomalous Capital Market Conditions
3. Incentive Adder for RTO Participation
4. Affiliate Adoption of Formula Rate (including ROE)
5. Pending Proposals Regarding Order 1000
6. Breaking News

COMBINED EFFECT OF FERC'S INCOME TAX ALLOWANCE POLICY AND THE DCF METHODOLOGY

- Background: FERC's Income Tax Allowance policy has a long and tortuous history.
- “FERC has not provided sufficient justification for its conclusion that there is no double recovery of taxes for partnership pipelines receiving a tax allowance in addition to the discounted cash flow return on equity.”
 - *United Airlines, Inc. v. FERC*, 827 F.3d 122, 136 (D.C. Cir. 2016).
- FERC's remand is expressly not limited to pipelines.
 - *Inquiry Regarding the Commission's Policy for Recovery of Income Tax Costs*, Docket No. PL17-1, 157 FERC ¶ 61,210 at PP 2, 19 (2016).

ANOMALOUS MARKET CONDITIONS

- Background: Opinion No. 531 determined that “unique” and “anomalous” capital market conditions undermined “mechanical application” of the DCF’s midpoint in setting ROE. Thus, FERC set the base ROE at the midpoint of the upper half of the zone of reasonableness.
 - *See Coakley v. Bangor Hydro-Elec. Co.*, Opinion No. 531, 47 FERC ¶ 61,234 at PP 142, 145, 150 (2014), *order on paper hearing*, Opinion No. 531-A, 149 FERC ¶ 61,032 (2014), *order on reh’g*, Opinion No. 531-B, 150 FERC ¶ 61,165 at PP 49-50, 56 (2015).

- “[I]n placing the base ROE within the zone of reasonableness, FERC failed to establish a ‘rational connection’ between the record evidence and its decision.”
 - *Emera Maine v. FERC*, 854 F.3d 9, 29 (D.C. Cir. 2017).

INCENTIVE ADDER FOR RTO PARTICIPATION

- Background: EAct 2005 and Order No. 679
- FERC routinely approves a 50 basis point ROE adder for continued RTO participation.
 - *Pac. Gas & Elec. Co.*, 148 FERC ¶ 61,245 at P 30 (2014), *order denying reh'g*, 154 FERC ¶ 61,119 at PP 10-13 (2016).
- *CPUC v. FERC*, Ninth Circuit Case No. 16-70481.
 - Oral argument is in two days.

AFFILIATE ADOPTION OF FORMULA RATE (INCLUDING ROE)

- Background: New transmission developers formed solely to compete for, finance, and construct Order 1000 Transmission Projects.
- FERC has approved multiple requests for “formula rate replication” by affiliates without a Section 205 filing.
 - *Transource Kansas, LLC*, 151 FERC ¶ 61,010 at PP 81-82 (2014), *order on reh’g and compliance*, 154 FERC ¶ 61,011 at PP 17-18 (2016).
 - *Kanstar Transmission, LLC*, 152 FERC ¶ 61,209 at PP 83-84 (2015), *order denying reh’g*, 155 FERC ¶ 61,167 at PP 9-10 (2016).
- *KCC v. FERC*, D.C. Cir. Case Nos. 16-1093/16-1164.
 - Oral argument is scheduled for November 20, 2017.

PENDING PROPOSALS REGARDING ORDER 1000

- Background: FERC decided “to discuss issues related to competitive transmission development processes, including but not limited to use of cost containment provisions, the relationship of competitive transmission development to transmission incentives, and other ratemaking issues.”
 - Docket No. AD16-18, *Competition Transmission Development Tech. Conf.*, Notice of Technical Conference (March 2016).

- Pending proposals in Docket No. AD16-18 include:
 - Pre-approving risk-reducing incentives;
 - Revising FERC’s incentive policy to encourage risk-mitigation measures;
 - Potential changes to FERC’s current application of the DCF methodology to better accommodate non-incumbent transmission developers, in particular with respect to the identification of appropriate proxy groups; and
 - A standard return on equity for non-incumbent Order 1000 project developers.

BREAKING NEWS

- Background: Secretary Perry's April 14, 2017 memorandum and DOE's August 23, 2017 "Grid Study" examined premature retirements of baseload units.
- Department of Energy's September 29, 2017 NOPR
 - Per Section 403 of the Department of Energy Organization Act, 42 U.S.C. § 7173.
 - *Grid Reliability and Resiliency Pricing*, Docket No. RM18-1
- Wholesale market issue, but any impact on ROE?

CONCLUSIONS AND TAKEAWAYS

- Success may require full FERC process and judicial intervention—develop your strategies and expectations accordingly.
- Pay attention to case-specific proposals in other regions—they may serve as the basis for approving proposals in your region.
- Pay attention to developments in other industries—they may have broad or ripple effects.
- Beware of “whack-a-mole” effect.

RESOURCES

- *United Airlines, Inc. v. FERC*, 827 F.3d 122 (D.C. Cir. 2016).
 - [https://www.cadc.uscourts.gov/internet/opinions.nsf/034AB41AC788112485257FE30050BB3F/\\$file/11-1479-1622707.pdf](https://www.cadc.uscourts.gov/internet/opinions.nsf/034AB41AC788112485257FE30050BB3F/$file/11-1479-1622707.pdf).
- *Inquiry Regarding the Commission's Policy for Recovery of Income Tax Costs*, Docket No. PL17-1, 157 FERC ¶ 61,210 (2016).
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=14435403>.
- *Emera Maine v. FERC*, 854 F.3d 9, 29 (D.C. Cir. 2017).
 - [https://www.cadc.uscourts.gov/internet/opinions.nsf/A6686ED29D2BFA7785258102004F179E/\\$file/15-1118-1671102.pdf](https://www.cadc.uscourts.gov/internet/opinions.nsf/A6686ED29D2BFA7785258102004F179E/$file/15-1118-1671102.pdf).

RESOURCES, CONT.

- *Pacific Gas & Electric Co.*, Docket No. ER14-2529.
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=13647456> (Hearing Order).
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=14148954> (Rehearing Order).

- *Transource Kansas, LLC*, Docket No. ER15-958.
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=13828729> (Hearing Order).
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=14094356> (Rehearing Order).

- *Kanstar Transmission, LLC*, Docket No. ER15-2237.
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=13989027> (Hearing Order).
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=14251587> (Rehearing Order).

RESOURCES, CONT.

- *Competitive Transmission Development Rates Technical Conference*, Docket No. AD16-18.
 - <https://elibrary-backup.ferc.gov/IDMWS/common/opennat.asp?fileID=14250105> (March 17, 2016 Notice).
 - <https://elibrary-backup.ferc.gov/IDMWS/common/opennat.asp?fileID=14322741> (August 3, 2016 Notice Inviting Comments).

- *Grid Reliability and Resiliency Pricing*, Docket No. RM18-1.
 - <https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=14696057> (September 29, 2017 NOPR).