125 FERC ¶ 61,183
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Northeast Utilities Service Company and National Grid USA — Docket No. ER08-1548-000

ORDER GRANTING INCENTIVE RATE TREATMENTS AND ACCEPTING ASSOCIATED TARIFF AMENDMENTS

(Issued November 17, 2008)

1. Northeast Utilities Service Company (Northeast Utilities), on behalf of its transmission-owning affiliates, and National Grid USA (National Grid), on behalf of its wholly-owned public utility subsidiaries (collectively, Applicants),[1] submitted an application, pursuant to sections 205 and 219 of the Federal Power Act (FPA),[2] and Order Nos. 679 and 679-A,[3] requesting approval of transmission rate incentives and associated tariff amendments for their comprehensive regional transmission project known as the New England East-West Solution (the Project). Applicants seek three incentives: (1) an incentive return on equity (ROE) of 150 basis points; (2) inclusion of 100 percent Construction Work in Progress (CWIP) costs in rate base; and (3) recovery of 100 percent of prudently incurred costs if the Project is abandoned for reasons beyond the control of Applicants. For the

[1] Northeast Utilities' transmission-owning affiliates are: The Connecticut Light and Power Company (Connecticut Light), Western Massachusetts Electric Company (Western Mass. Electric), Public Service Company of New Hampshire, Holyoke Power and Electric Company, and Holyoke Water Power Company. National Grid's wholly-owned public utility subsidiaries are: The Narragansett Electric Company (Narragansett) and New England Power.

[2] 16 U.S.C. §§ 824d, 824s (2006).

[3] *Promoting Transmission Investment through Pricing Reform*, Order No. 679, FERC Stats. & Regs. ¶ 31,222, *order on reh'g*, Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 (2006), *order on reh'g*, 119 FERC ¶ 61,062 (2007).

reasons discussed below, with one modification, we grant Applicants' requested incentive rate treatments and accept the associated proposed tariff amendments, effective November 18, 2008.

I. Background

2. Applicants describe the Project as a complex addition to the New England 345-kV transmission system aimed at substantially improving the reliability of electric transmission service in southern New England. It is a large-scale, regional transmission solution involving improvements to the transmission system of two New England transmission owners. Specifically, the Project comprises what the Applicants describe as "four inter-related components and several related and necessary upgrades" across three states: (1) the Greater Springfield Reliability Project (Springfield Component); (2) the Interstate Reliability Project (Interstate Component); (3) the Central Connecticut Reliability Project (Connecticut Component); and (4) the Rhode Island Reliability Project (Rhode Island Component).[4] Each of the individual components has a tentative in-service date of 2012 or 2013.[5]

3. The Springfield Component is a group of system reinforcements to upgrade the transmission system of Connecticut Light and Western Mass. Electric in Connecticut and Massachusetts. The Springfield Component consists of a proposal to build upgrades to both the 115-kV system that transmits power among substations that serve local load, as well as to the 345-kV bulk power supply system by adding a second 345-kV line between Massachusetts and Connecticut. The two companies will also perform major station upgrades in Connecticut and Massachusetts and construct two new switching substations in Greater Springfield, Massachusetts. Connecticut Light will construct and own the portions of the Springfield Component located in Connecticut, and Western Mass. Electric will construct and own the portions of the project located in Massachusetts. The Springfield Component is expected to cost approximately $714 million and be fully in service in 2013.[6]

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[4] Joint Application Transmittal Letter (the Transmittal Letter) at 9.

[5] *See id.* at 10-12.

[6] *Id.* at 10.

4. The Interstate Component of the Project is a joint project between Connecticut Light and National Grid (Narragansett and New England Power)[7] that will include construction of a new interstate 345-kV line from Massachusetts, continuing through Rhode Island, and terminating in Connecticut, in order to strengthen the ties between those three states. The Interstate Component comprised of approximately 77 miles of new 345-kV lines as well as improvements to existing 345-kV and 115-kV facilities at an estimated cost of $457 million. The Interstate Component is expected to be completed and placed in service in 2012 or 2013.[8]

5. The Connecticut Component involves proposals for a new 345-kV transmission line in central Connecticut as well as a new 38-mile-long 345-kV line from Connecticut Light's (Northeast Utilities) North Bloomfield Substation to its Frost Bridge Substation in Watertown. This proposal also calls for many improvements to existing 345-kV and 115-kV facilities including the installation of a second 345/115-kV autotransformer between Massachusetts and Connecticut. Applicants state that the Connecticut Component will improve the east-west transfer capability in Connecticut, and when combined with the Springfield Component, will establish an independent 345-kV interconnection between western Massachusetts and Connecticut. Moreover, Applicants state that the Connecticut Component will add diversity to the system by establishing a new source west of Southington Station, bringing bulk power closer to customer load. The anticipated cost of the Connecticut Component is $313 million. It is scheduled to be completed and placed in service in 2013.[9]

6. The Rhode Island Component, which is to be constructed by National Grid, is a proposed upgrade on an existing right-of-way running north-south from North Smithfield to Warwick in Rhode Island. This includes an additional 345-kV line between the West Farnum (North Smithfield) and Kent County (Warwick) substations as well as the installation of an additional 345/115-kV autotransformer at an existing substation.[10] The Rhode Island Component would also involve a significant amount of "reconductoring" of various segments of 115-kV lines and

[7] Unless otherwise noted, references to National Grid herein are intended to refer to Narragansett and New England Power.

[8] Transmittal Letter at 11.

[9] *Id.* at 11-12.

[10] *Id.* at 12.

terminal equipment upgrades. Applicants anticipate that these additional transmission lines and other upgrades will cost $285 million.[11] The Rhode Island Component also consists of additional upgrades that National Grid asserts must be constructed and placed in service in advance of other updates in the Rhode Island Component in order to avoid overloads of the existing transmission network and to allow for system outages when the major Rhode Island Component upgrades are constructed.[12] These upgrades include installation of an additional Kent County 345/115-kV auto transformer; two 115-kV, 72-MVAR capacitors and other upgrades to the Kent County Substation; and a new 345/115-kV Plainville Substation, as well as the upgrade of 115-kV lines and substation equipment.[13] These upgrades are projected to cost approximately $143 million in total. The Rhode Island Component is expected to be completed and placed in service in late 2012.[14]

7. The Project has an overall estimated cost of $2.1 billion. Northeast Utilities' share has been estimated at $1.49 billion, and National Grid's share $634 million. Applicants say that in dollar terms, the Project is among the largest transmission infrastructure projects that they have pursued and that the sizeable investments in the Project will impose a significant strain upon the Applicants' financial resources. Applicants also argue that as a transmission solution that crosses three states, the Project faces special siting and permitting risks and challenges because it requires regulatory approvals from multiple states.

A. Requested Incentives

8. First, Applicants each seek rate incentive adders of 150 basis points to their base ROE,[15] and they argue that the requested 13.14 percent ROE will help to offset some of the siting, regulatory, and financial risks by helping to attract the necessary capital investment for the Project by offering a return for investors

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[11] *Id.*

[12] *Id.*

[13] *Id.*

[14] *Id.*

[15] All of the affected companies have the same base ROE per *Bangor Hydro-Electric Co.*, 117 FERC ¶ 61,129 (2006) (Opinion No. 489); *order on reh'g*, 122 FERC ¶ 61,265 (2008) (Opinion No. 489 Rehearing Order).

commensurate with those risks. Second, Applicants argue that their 100 percent CWIP recovery will provide up-front regulatory certainty and rate stability, improve cash flow, and provide a more prompt return on investments, which would enhance their credit quality and debt ratings. Applicants assert that this rate treatment would be necessary to offset the financial risks associated with the Project and to attract needed investments. Finally, Applicants seek abandoned plant recovery in the event that one or more components of the Project are abandoned for reasons beyond their control.

9. Applicants argue that the requested incentives meet the Commission's nexus test for eligibility for incentives under section 219 for three reasons: first, the Project is the product of the regional planning process in New England, which has been Commission-approved as a fair and open planning process;[16] second, there is substantial evidence to demonstrate that the Project will significantly improve transmission reliability in southern New England; and third, because the total package of incentives requested is tailored to address the demonstrable risks or challenges faced by the Project. Applicants also argue that the resulting rates would be just and reasonable for three reasons: first, the 13.14 percent ROE is within the zone of reasonableness approved in Order No. 489;[17] second, the inclusion of CWIP in rate base affects only the timing of cost recovery and not the amount because the capitalization of allowance of funds used during construction (AFUDC) will be replaced by CWIP in the rate base; and third, recovery of abandoned plant costs will only be requested from the Commission if needed.

1. 13.14 Percent ROE

10. The requested 13.14 percent ROE represents a 150 basis point increase from the base ROE of 11.64 percent approved by the Commission for New England Transmission Owners pursuant to the Commission's orders in Docket No. ER04-157. [18] First, Applicants argue the magnitude of the Project will impose significant financial risks. For instance, the financial condition of Northeast

[16] *See ISO New England Inc.*, 106 FERC ¶ 61,280, *order on reh'g, ISO New England Inc.*,109 FERC ¶ 61,147 (2004); *ISO-New England Inc.*, 123 FERC ¶ 61,161, at P 23 (2008) (finding that the ISO-NE Regional System Plan process satisfies the openness and coordination principles of Order Nos. 890 and 890-A).

[17] Opinion No. 489, 117 FERC ¶ 61,129 at P 14.

[18] Opinion No. 489 Rehearing Order at P 9-13; 19-22.

Utilities affiliates that are involved in the project, Connecticut Light and Western Mass. Electric is already heavily strained due to their unprecedented capital expansion program over the past several years.

11. Further, in 2005, credit rating agencies, including Standard & Poor's and Moody's, downgraded the Northeast Utilities' credit ratings on all of their securities. These downgrades occurred in significant part because of the risks in Connecticut Light's large construction program to expand and upgrade its transmission and distribution system in Connecticut and the impact of those capital expenditures on the financial ratios of Connecticut Light and its parent company. As to National Grid, such a large capital expenditure places significant pressure on its credit ratings. These risks are exacerbated by the fact that Moody's has placed National Grid on negative outlook. Applicants argue that the ROE incentive requested in this filing mitigates this risk.

2. CWIP

12. Applicants assert that 100 percent CWIP in rate base will alleviate further downward pressures on the Northeast Utilities' and National Grid's financial health. As an example, Applicants point out that during the construction period for the Project, Connecticut Light and Western Mass. Electric's cash flows will be negative. They explain a cash flow shortage can adversely affect a utility's coverage ratios and reduce its credit ratings. That would, in turn, likely increase the cost of borrowing capital to help finance construction. Applicants further explain that 100 percent CWIP recovery will improve Connecticut Light's and Western Mass. Electric's cash flows by approximately $137 million during the construction period and reduce the amount of debt financing that Connecticut Light and Western Mass. Electric will need to obtain.

13. Applicants also assert that 100 percent CWIP recovery will improve National Grid's cash flows during the construction period. They say National Grid's cash flows will be significantly impacted by the capital outlay required for the Project. Such cash flow pressure can significantly depress key financial ratios used by ratings analysts during the construction period, greatly increasing the probability of a ratings downgrade. Applicants say this is a particular risk to National Grid, because Moody's has placed all of National Grid's ratings on negative outlook, which means they consider there to be a 25-50 percent chance of a downgrade within the next 12-18 months.

14. Further, the credit rating agencies have emphasized the importance of Northeast Utilities' ability to obtain CWIP recovery for the Project. Applicants state in an August 8, 2008 ratings report that Fitch Ratings stressed that adequate

cash flow earnings through CWIP will be "vital" to Northeast Utilities' credit ratings, especially as they undertake the Project upgrades. Also, Applicants state that granting 100 percent CWIP will help them raise equity and debt capital from investors who may otherwise be discouraged by long delays in the recovery of expenses. Applicants argue the Commission has recognized that the investment community views CWIP as more favorable than AFUDC.[19] The Applicants also argue the Commission has previously granted the 100 percent CWIP incentive to help the construction of large-scale transmission projects.[20]

15. In their application, the Applicants describe the accounting controls they will use to prevent charging customers for both capitalized AFUDC and corresponding amounts of CWIP in rate base associated with the Project prior to and after the project goes into service. Specifically, Northeast Utilities explains that it will use its Management Information & Budgeting System (MIBS) to track transmission projects before the projects are placed into service. [21]

16. As part of the monthly closing of CWIP work orders, Northeast Utilities will determine the amount of AFUDC recorded on transmission work orders associated with the Project. Northeast Utilities will then record a regulatory liability in Account 254, Other Regulatory Liabilities, for 100 percent of the AFUDC recorded on the Project and treat the regulatory liability as an offset to rate base. Northeast Utilities also propose to amortize the regulatory liability to Account 407.4, Regulatory Credits, over the average life of assets in service as an offset to depreciation expense.

17. Similar to Northeast Utilities' accounting procedures, National Grid states that New England Power – a subsidiary of National Grid - will accrue AFUDC on the Project assets in Massachusetts and record a regulatory liability for the full

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[19] *See e.g., United Illuminating Co.*, 119 FERC ¶ 61,182, at P 63 (2007) (UI Incentive Order) (noting that "CWIP is viewed more favorably by investors than AFUDC") (citing *Construction Work In Progress for Pub. Utils.; Inclusion of Costs in Rate Base*, Order No. 298, FERC Stats. & Regs. ¶ 30,455, at 30,495 *order on reh'g*, Order No. 298-A, FERC Stats. & Regs. ¶ 30,500, at 30,724 (1983), *order on reh'g*, Order No. 298-B, FERC Stats. & Regs. ¶ 30,524 (1983).

[20] *Id.* P 66 ("The Commission also agrees with UI that allowing the 100 percent CWIP incentive will help ensure completion of the Project").

[21] *See* Affidavit of Ms. Pamela A.Viapiano (Exhibit NU/NG 500, p.9).

amount of AFUDC recorded, as an offset to rate base. Additionally, the regulatory liability will be amortized over the average life of the projects and will be included as an offset to depreciation expense in the Schedule 21-New England Power revenue requirement.

18. National Grid also explains that Narragansett will implement different accounting procedures for the Project assets in Rhode Island. For Narragansett, National Grid states it will not accrue AFUDC for the portion of the Project in Rhode Island. National Grid explains that all the Project work orders associated with investment in Rhode Island will be monitored and specifically marked in its utility accounting system to ensure that AFUDC is not accrued on these work orders.

3. Abandonment

19. In addition to the two incentives outlined above designed to mitigate cash flow and revenue risks and their relative impacts on the Applicants' financial health (through CWIP and ROE, respectively), Applicants seek the ability to recover 100 percent of prudently-incurred abandoned plant costs if the Project were to be abandoned for any reason outside of Applicants' control. Applicants argue this additional protection is narrowly tailored to address a separate risk not addressed by ROE or CWIP - the risk of unrecovered costs due to non-completion. Applicants cite to Order No. 679, arguing that it permits the recovery of 100 percent of prudently incurred costs associated with abandoned transmission projects "if such abandonment is outside the control of management," as such incentive is an "effective means to encourage transmission development by reducing the risk of non-recovery of costs."[22] Applicants cite to Commission precedent to note this incentive is especially appropriate where a transmission project can be cancelled by a regional transmission organization (RTO) to which the applicant belongs.[23]

20. Applicants argue authority to recover abandoned plant costs is particularly important and warranted for the Project due to the much higher than normal levels

[22] Order No. 679, FERC Stats. & Regs. ¶ 31,222, at P 163.

[23] *See PPL Electric Utilities Corp.*, 123 FERC ¶ 61,068, at P 47, *reh'g denied*, 124 FERC ¶ 61,229 (2008).

of approvals upon which the Project's ultimate completion depends.[24] With such intense permitting and siting obligations, the risks to final completion for the Project are much greater than for a routine transmission investment. Therefore, due to the massive commitment of capital required, the financial risk to the Applicants of losing abandoned plant costs is correspondingly high. They state the Commission has previously determined that "dependence upon approval by multiple jurisdictions introduces a significant element of risk" not faced by utilities constructing transmission projects within a single jurisdiction.[25] Applicants argue that in *SCE* the Commission also determined that allowing recovery of abandoned plant costs was appropriate because *SCE* had not yet received certain regulatory approvals for its project. Accordingly, recovery of abandoned plant costs is appropriate for the Project as a layer of financial protection not provided by the incentives requested above. As the Commission has recognized, "the recovery of abandonment costs is an effective means of encouraging transmission development by reducing the risk of non-recovery of costs."[26]

21. Of note, Applicants claim that under the terms of the transmission operating agreement (TOA), they already have the right to recover prudently-incurred abandoned plant costs if ISO-NE removes the Project from the Regional System Plan after directing the Applicants to move forward with the construction.[27] Due to the historic scope and size of the Project, the Applicants request abandoned plant recovery as an incentive under Order No. 679, notwithstanding the protection afforded by the TOA. Because the Applicants believe that the Project qualifies for abandoned plant recovery under Order No. 679, they explain that the Commission need not address issues regarding the scope of the TOA's abandoned plant provisions in order to take action on the instant rate filing.

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[24] Applicants explain that this Project involves two utility systems in three states, three state siting commissions, and a host of state regulatory authorities. *See infra*. P 29-35.

[25] *Southern California Edison Co.*, 121 FERC ¶ 61,168, at P 72 (2007) (*SCE*).

[26] *Pac. Gas & Electric Co.*, 123 FERC ¶ 61,067, at P 36, (2008) (citing Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 163).

[27] *See* section 1.1(d) of Schedule 3.09(a) of TOA.

B. Eligibility for ROE, CWIP, and Abandonment Incentives

22. Applicants acknowledge that in order to receive incentives under Order No. 679, an applicant must show that its project is eligible for incentives under section 219 of the FPA[28] because it either ensures reliability or reduces the cost of delivered power by reducing transmission congestion. Applicants further acknowledge that in addition to satisfying the section 219 requirement, an applicant must also demonstrate that there is a nexus between the incentive sought and the investment being made and that the total package of incentives requested is tailored to address the demonstrable risks and challenges that the applicant faces in undertaking the Project.

1. Section 219 Requirement

23. Applicants claim that the Project is presumptively eligible for incentives under section 219 of the FPA. First, they argue that the Project is entitled to the rebuttable presumption because it is the product of the regional planning process in New England, which, as noted above, the Commission has approved as a fair and open planning process.[29] Applicants state the system reliability problems associated with the Project were first identified in the ISO-NE's 2003 Regional System Plan. The development of the Regional System Plan, which is approved by the ISO-NE Board of Directors, involves the participation of the ISO-NE's Planning Advisory Committee.[30] Further, as part of the New England regional planning process, ISO-NE evaluates the reliability and congestion benefits of a

[28] 16 U.S.C. § 824s (2006).

[29] *See e.g., ISO-New England Inc.*, 123 FERC ¶ 61,161, at P 23 (2008); *see also Northeast Utilities Service Company*, 124 FERC ¶ 61,044, at P 67 (2008) ("the Middletown-to-Norwalk Project satisfies the section 219 requirements because the project ensures reliability and/or reduces congestion costs. Northeast Utilities is entitled to a rebuttable presumption regarding this fact based on the review and approval of the Middletown-to-Norwalk Project by ISO-New England"); *UI Incentive Order*, 119 FERC ¶ 61,182, at P 58 (2007) (finding UI qualifies for the rebuttable presumption that the Project ensures reliability or reduces the cost of delivered power based on the detailed studies and analyses done by ISO-NE and the findings of the Connecticut Siting Council).

[30] The Planning Advisory Committee is a stakeholder body that comprises transmission planners, electricity market participants, customers, representatives from governmental entities, and various officials in the New England states.

proposed transmission project. Accordingly, because the Project is included in the ISO-NE Regional System Plan, Applicants argue it is entitled to the rebuttable presumption that it satisfies the requirements of section 219.

24. Applicants also argue that the Project is eligible for incentives because there is substantial evidence to demonstrate that the Project will significantly improve the southern New England's transmission reliability. Applicants argue it is known that there are significant reliability problems in the southern New England transmission system, and that the Project is intended to address these problems. The Springfield Component is intended to improve the currently weak 115-kV system through and around the Greater Springfield area and to create a 345-kV "loop" through north central Connecticut and eastern Massachusetts. This loop will relieve congestion on the existing 115-kV system and increase the power transfer capacity between Massachusetts and Connecticut. The Interstate Component will strengthen the ties among Massachusetts, Rhode Island and Connecticut to enable the transmission system serving this tri-state area to meet reliability standards, as well as providing each state with access to competitive power markets and potential access to renewable energy sources. The Connecticut Component will improve the reliability and capacity for the transfer of power between eastern and western Connecticut, as well as provide a number of other reliability benefits. Finally, the Rhode Island Component will address several serious reliability concerns, including the fact that Rhode Island's reliability is compromised because it is currently overly-dependent upon local generation and has limited access to the 345-kV system, resulting in overloads and voltage violations.

2. Order No. 679 Nexus Requirement

25. The Applicants request a package of incentives that they argue is tailored to offset the specific risks and challenges associated with the Project. Taken as a package, Applicants say these incentives are designed to offset the substantial risks and challenges presented by an undertaking of this magnitude in order to sufficiently attract investments in the Project and ensure its completion.

a. Scope

26. Applicants state that the Project is a major transmission project that will span three states and affect the transmission systems of two New England transmission owners. In dollar terms, the Project will have a combined estimated cost of $2.1 billion. Specifically, Northeast Utilities' share is $1.409 billion and

National Grid's share is $634 million. Applicants state this represents an enormous financial commitment for them.[31]

b. Effects

27. Applicants assert that the Project will have significant reliability benefits for the transmission system in Massachusetts, Connecticut and Rhode Island, and indeed for New England as a whole.[32] It will upgrade and expand the region's 345-kV backbone transmission, will ensure that the southern New England grid is reliable and complies with the reliability standards of North American Electric Reliability Corporation, Northeast Power Coordinating Council, and ISO-NE. Applicants explain that southern New England is in great need of system upgrades, and the current situation is such that the region's transmission system will be in violation of reliability standards by as early as 2009 if improvements are not made. Indeed, problems in the Greater Springfield area exist today. Applicants argue the Project is a regional solution that will increase the reliability and capacity for power transfers across the New England power grid, as well as address multiple reliability issues.

28. Applicants state the Project will work to resolve a number of reliability problems in New England as a whole, including increasing east-west transfer capability and strengthening interconnections between Massachusetts, Rhode Island and Connecticut.[33] On a state-by-state basis, the Project will benefit Massachusetts by solving Greater Springfield reliability problems and providing reliability support to the West Medway area through the creation of a 345-kV loop in eastern Massachusetts. In Connecticut, the Project will increase interstate transfer capability, as well as East-West transfer capability. Finally, Rhode Island will benefit from a reduction in reliability problems and the creation of new 345-kV interconnections.

c. Risks and Challenges

29. Applicants assert they face significant financial risks associated with the Project. This is a massive undertaking for both Applicants.[34] For Northeast

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[31] Transmittal Letter at 16-17.

[32] *Id.* at 17.

[33] *Id*. at 17-18.

[34] *Id.* at 17-19.

Utilities, the heavy capital requirements for the Project will perpetuate the relatively weak financial conditions suffered by its affiliates, Connecticut Light and Western Mass. Electric. Over the past several years, these affiliates have been investing large amounts of capital to upgrade their transmission and distribution systems, which has imposed significant pressure on their financial profiles. Applicants explain that Northeast Utilities and its subsidiaries' credit ratings were downgraded by the various rating agencies in 2005 because of their weak credit metrics and financial ratios. Applicants state the large investments that Connecticut Light and Western Mass. Electric will make in the Project will perpetuate their weak financial condition, particularly because the construction of the Project involves a lengthy, multi-year process with a final in-service date of 2013. Given the financial strain imposed by the capital expenditure program, Applicants assert that higher credit ratings are precluded at this time.

30. Moreover, Applicants state the Project will face internal competition for financing with other projects that are part of Northeast Utilities' and National Grid's capital expenditure programs. The large dollar investments required for the Project will cause significant strain on the Applicants' financial condition and therefore will cause greater internal scrutiny and internal competition for financing.

31. Applicants state that the Project faces multiple regulatory risks associated with siting and permitting authorization, as well as public opposition to the routing of the Project components.[35] Applicants cite Opinion No. 489[36] to argue that hurdles facing new transmission projects can include regulatory approvals, expenditure of political capital, siting delays, zoning regulations, land use requirements and public opposition. The Project faces significant siting and permitting risks as a result of the need to obtain multiple state, federal, and local approvals.

32. Because the Project is subject to regulatory approval processes in three different states, Applicants contend it faces the possibility of inconsistent and conflicting approval conditions, which would require additional proceedings to resolve. Specifically, the Project will need to undergo a comprehensive siting process before the Connecticut Siting Council, the Massachusetts Energy Facilities Siting Board, and the Rhode Island Energy Facility Siting Board, which will consider numerous factors, including alternatives to each of the projects (such as

[35] *Id.* at 19-20.

[36] 117 FERC ¶ 61,129 at P 105.

route alternatives, potential environmental and social issues, electric and magnetic field issues, engineering designs, costs, etc.). Further, prior to actually submitting siting applications, Northeast Utilities and National Grid must engage in a municipal consultation process that is designed to obtain input and comments from the public and local government representatives in each of the Connecticut, Massachusetts, and Rhode Island municipalities in which the preferred or alternative routes of the proposed Project are located.

33. In addition to the siting approvals, the Project will require numerous other permits at the federal, state, and local level in all three states. This includes several municipal agencies and state commissions as well as various federal agencies and departments. If any municipal, state, or federal agency does not grant a required regulatory approval, one or more portions of the Project could be delayed or abandoned.

34. Applicants claim that the Project faces engineering and construction challenges. For example, the Project requires coordinating between two New England transmission owners located in three states in order to develop, site, and construct this large-scale transmission project. Applicants note that a major challenge in the Project's construction will be the coordination and sequence of transmission outages necessary to make the necessary additions to the transmission system. Also, obtaining the needed rights-of-way for the construction of the Project presents other risks and challenges.

35. Finally, Applicants argue that the Project faces significant procurement and labor risks in the construction of the Project. Applicants state that because of the increased demand for transmission-related labor, materials, and equipment due to new transmission construction throughout the country, the timely delivery of construction materials and availability of skilled labor creates risks for the Project in terms of costs and schedules. Specifically, the lead times required to procure many construction components for the Project have lengthened to the point where it may be necessary for the Applicants to purchase construction materials early in the planning and development process.

C. Technology Statement

36. Order No. 679 requires applicants for incentive rate treatments to include a technology statement describing the advanced technologies that have been considered and, if not employed, an explanation of the reasons why they were

not.[37] Applicants state that they will employ several advanced technologies in the construction of the components of the Project as discussed in the Transmittal Letter and the accompanying testimony and exhibits. Specifically, the Project employs fiber optic technologies, 64 high-temperature conductors, aerial laser survey technology, and power electronics and related software (including real time monitoring and analytical software). In addition, certain National Grid portions of the Project use a high-temperature aluminum conductor steel supported conductor.

D. Tariff Revisions

37. The Applicants intend to recover the proposed 13.14 percent ROE incentive through regional network service rates in accordance with the currently pending tariff revisions in Docket No. ER04-157 and under New England Power's Tariff No. 1. Applicants have included proposed changes to Schedule 21-NU to implement 100 percent CWIP recovery for the Project in their application. Similar are the proposed changes to Schedule 21-New England Power and New England Power's Tariff No. 1 to implement 100 percent CWIP Recovery.

II. Notice of Filing and Responsive Pleadings

38. Notice of the filing was published in the *Federal Register*,[38] with comments and interventions due on or before October 8, 2008. The New England Conference of Public Utilities Commissioners, Inc. (NECPUC), and the Maine Public Utilities Commission (Maine Commission) filed timely notices of intervention and a joint motion for an extension of time to file comments. A notice of extension of time was issued on October 6, 2008, extending the comment date to October 14, 2008. The Attorneys General of the State of Connecticut (Connecticut AG), the State of Rhode Island (Rhode Island AG), and the Commonwealth of Massachusetts (Mass. AG), the Connecticut Office of Consumer Counsel (Connecticut Consumer Counsel), The United Illuminating Company, the Chicopee Municipal Lighting Plant and South Hadley Electric Light Department (collectively, Chicopee and South Hadley), the NRG Companies (NRG), and the Massachusetts Municipal Wholesale Electric Company (MMWEC) filed timely motions to intervene. The Connecticut Department of Public Utility Control (Connecticut Department) and the Massachusetts

[37] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 302.

[38] 73 Fed. Reg. 56,811 (2008).

Department of Public Utilities filed notices of intervention. The Vermont Department of Public Service (the Vermont Department) filed a motion to intervene out of time and protest.

39. The Maine Commission, the NECPUC, the Rhode Island AG, and the Connecticut Department (Joint Protesters) jointly submitted a motion to hold the Applicants' application in abeyance and a protest. [39] MMWEC, the Connecticut AG, the Mass. AG, Chicopee and South Hadley, and NRG all filed separate protests. Applicants filed an answer to the Joint Protesters' motion and an Answer to the Comments and Protests.

III. Discussion

A. Procedural Matters

40. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,[40] the timely, unopposed motions to intervene and notices of intervention serve to make the entities that filed these motions parties to this proceeding. The Vermont Department's motion to intervene out of time is granted.

41. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure[41] prohibits an answer to a protest and/or answer unless otherwise ordered by decisional authority. We will accept Applicants' answer because it has provided information that has assisted us in our decision-making process.

B. Substantive Matters

1. Motion to Hold Application in Abeyance

a. Joint Protesters

42. The Joint Protesters filed a motion requesting that the Commission hold Applicants' application in abeyance pending the Project receiving the requisite Certificates of Need from the states involved.

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[39] The Vermont Department filed a protest adopting the arguments of the Joint Protesters.

[40] 18 C.F.R. § 385.214 (2008).

[41] *Id.* § 385.213(a)(2).

43. The Joint Protesters state that holding Applicants' petition in abeyance will ensure that the Commission has the benefit of the states' extensive review of the Project, guarantee that the Commission reviews the Project in its final form, and avoid the administrative inefficiency of the Commission having to revisit its decision if the facts on which it relied in adjudicating the Project change as a result of the Certificate of Need proceedings.

44. The Joint Protesters argue that the Commission should not encourage the transmission owners' "gold rush" at the expense of consumers, especially in view of the current financial crisis. Holding this application in abeyance will allow a deliberate approach to the requests once all the facts are in place and the financial situation has stabilized.

45. Finally, the Joint Protesters argue that holding the application in abeyance is consistent with the Commission's intent, expressed in Order Nos. 679 and 679-A, to coordinate its consideration of incentives with the state siting authority.[42] Finally, the Joint Protesters state that unless the Commission holds the petition in abeyance, the Maine Commission cannot contest the Project's merits without prejudging the pending Certificate of Need proceeding.

b. Answer

46. Applicants argue this request is meritless, is contrary to Commission policy and precedent, and should be rejected out of hand. First, they note the Commission recently rejected the identical argument when the Joint Protesters and other Intervenors raised it in another New England transmission owner's incentive application.[43] The Commission's rationale in rejecting abeyance requests in *Central Maine* is equally applicable to the Project incentive request.

47. Second, Applicants argue Order No. 679 does not require an applicant seeking incentive ratemaking to complete the state review process before submitting an application with the Commission. To the contrary, Applicants note Order No. 679 states that parties proposing to build new transmission projects

[42] Joint Protesters' Motion for Abeyance and Protest at 8 (citing Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 54; Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 5) (Joint Protesters).

[43] *See* Applicants' October 24 Answer at 5, citing *Central Maine Power Co.*, 125 FERC ¶ 61,079 (2008) (*Central Maine*).

have the ability to obtain upfront Commission guidance on their incentive request before making a decision as to whether to proceed with the project.[44]

48. Third, Applicants argue under Order No. 679 that the Commission does not need specific project parameters that may be approved in the state siting proceedings in order to determine whether a project is eligible for incentive rate treatment.[45] Further, the Commission will not need to revisit its original incentive order once the state siting processes have been completed. Applicants argue that state siting approval is relevant only to the extent that it affords the applicant a rebuttable presumption that the project ensures reliability or reduces congestion.

49. Finally, Applicants argue the Joint Protesters' motion to hold the filing in abeyance is especially inappropriate when directed to a filing under section 205 of the FPA. The Applicants have the right under the FPA, the TOA and the ISO-NE Tariff to file changes to their transmission rates and to put those changes into effect after providing the requisite notice. [46] Applicants say the Joint Protesters' motion improperly seeks to countermand the Applicants' exercise of that right and to extend unilaterally the notice period before the revised rates take effect.

c. Commission Determination

50. We deny the motion. The Commission decides petitions for incentives pursuant to section 219 and Order No. 679 under different criteria than the states decide certificate of need applications. When faced with a request for incentives pursuant to section 219 and Order No. 679, the Commission examines whether the project reduces congestion or ensures reliability, and determines whether there is a nexus between the incentive sought and the investment being made. For example, as noted in *Central Maine*, the Commission explained that the Maine Commission would determine whether the project is needed—a different standard that permits inquiry into a broader range of issues.[47] Given these different standards, and the

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[44] *Id.* citing Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 25 ("[I]ncentives are ordinarily sought before investment decisions are made and, hence, before any siting impediments are even confronted" (emphasis omitted)).

[45] *Id.* at 7, citing Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 54.

[46] *Id*. citing FPA section 205(d) 16 U.S.C. § 824d(d); 18 C.F.R. § 35.3 (2008).

[47] 125 FERC ¶ 61,079, at P 39 (2008) (*Central Maine*).

different questions they raise, there is no risk that the Commission will prejudge any pending state certificate of need proceedings by ruling on its petition for incentives. Similarly, because the issues relevant to the Commission's decision are different than the issues relevant to the state regulators' decision, there is no significant increase in administrative efficiency to be gained by holding the petition in abeyance pending the outcome of the certificates of need proceedings.[48]

51. Moreover, as noted in *Central Maine*,[49] although construction cannot begin until the states rule on the Certificate of Need applications, a Commission decision on the petition will provide Applicants with a greater degree of certainty as they discuss their future financing needs with lenders and rating agencies. This is consistent with the goals of section 219, which directed the Commission to provide rate incentives that "promote reliable and economically efficient transmission . . . by promoting capital investment in the enlargement, improvement, maintenance, and operation of all facilities for the transmission of electric energy."[50]

2. Motions for Hearing and Suspension

a. Protest

52. Several Intervenors ask the Commission to set all or portions of the Applicants' request for incentive transmission rates for evidentiary hearing.[51] NRG, for example, states that a hearing is necessary to resolve the material facts in dispute as to whether the Project is really a collection of four separate projects, together with other system work, that in whole or in part should be

[48] There may be some overlap between the two inquiries insofar as approval of a certificate of need gives rise to a rebuttable presumption that a project satisfies section 219's eligibility requirement; however, certificate of need approval is neither necessary to satisfy the section 219 requirement nor sufficient to demonstrate that there is a nexus between the incentive sought and the investment being made.

[49] *Central Maine*, 125 FERC ¶ 61,079 at P 40.

[50] 16 U.S.C. § 824s(b)(1) (2006).

[51] Joint Protesters at 13; MMWEC at 22; Massachusetts AG at 9; Connecticut AG at 1; Chicopee at 2; NRG at 2.

considered to be routine and ineligible for incentives.[52] MMWEC similarly asks the Commission to set for hearing the adequacy of Applicants' demonstration of a "nexus" between the Project investment and the requested incentives.[53] MMWEC also asks the Commission to set for hearing the issue of the Applicants' contractual obligations under the New England TOA to construct necessary transmission.[54] Joint Protesters request that the ROE be set for hearing.[55]

b. Answer

53. The Applicants say they have demonstrated, through an extensive amount of testimony and exhibits, that regardless of whether the Project is viewed as a single, integrated project, or each Project component is analyzed separately, the Project and its components are anything but routine. They have demonstrated the nexus between the Project and the incentives with that same testimony and exhibits. Regarding the hearing requested on the ROE, Applicants argue it is not necessary because the requested ROE is within the acceptable range. Additionally, Applicants note that the Commission has previously stated that an application for an incentive ROE does not present an occasion for re-litigating the base ROE of the petitioning transmission owners.[56] Next, Applicants note that the precise issue of the Applicants being required to build necessary transmission under the TOA has already been resolved in other Commission decisions without a hearing.[57] Next, Applicants note that Chicopee and South Hadley and MMWEC, who request that the Applicants' incentive rates be suspended,[58] do not even attempt to show that the Applicants' filing would produce substantially excessive revenues warranting maximum suspension, defined as revenues that are more than

[52] NRG at 2.

[53] MMWEC at 22.

[54] *Id.*

[55] Joint Protesters at 13.

[56] *See Pepco Holdings, Inc*., 124 FERC ¶ 61,176, at P 123 (2008) (*Pepco*).

[57] *See e.g.*, Opinion No. 489 Rehearing Order, 122 FERC ¶ 61,265 at P 79.

[58] Chicopee and South Hadley at 3; MMWEC at 22-23.

10 percent excessive.[59] Finally, Applicants note that if the incentive rates were to be suspended as requested, they would primarily affect the Applicants' ability to include CWIP in rate base for the Project investments that take place during the suspension period. Applicants argue the Intervenors raise no substantial objection to the CWIP proposal and that, in any event, the inclusion of CWIP in rate base cannot produce substantially excessive revenues, since it represents only a timing difference.

c. Commission Determination

54. We deny protestors' request for a trial-type evidentiary hearing**.** These challenges are contrary to well established case law. Federal courts have held repeatedly that "a formal trial-type hearing is unnecessary where there are no material facts in dispute."[60] Since we do not, as discussed below, find such material issues of fact, we conclude it unnecessary to set this matter for hearing.

3. Section 219 Requirement

a. Protest

55. The Joint Protesters argue that the Commission should deny Applicants' petition because the Project fails to satisfy section 219's threshold criteria for incentive rate treatment. The Joint Protesters state that to be eligible for incentives under section 219, an applicant must show that its project either ensures reliability or reduces the cost of delivered power by reducing transmission congestion. The Joint Protesters assert that the Project does not currently qualify for either of these rebuttable presumptions because it has not received state siting approval.

b. Commission Determination

56. In Order No. 679, the Commission stated that an applicant for transmission incentives must demonstrate that the facilities for which it seeks incentives satisfy the requirements of FPA section 219 by either ensuring reliability or reducing the

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[59] *West Texas Utilities Co.,* 18 FERC ¶ 61,374 (1982) (*West Texas*); *see also Boston Edison Company*, 65 FERC ¶ 61,311, at 62,424 (1993); *Jersey Central Power & Light Company*, 56 FERC ¶ 61,376, at 62,436 n.1 (1991).

[60] *Pepco*, 124 FERC ¶ 61,176, at P 130 (citing *Pennsylvania Pub. Util. Comm'n v. FERC*, 279 U.S. App. D.C. 408, 881 F.2d 1123 (D.C. Cir. 1989).

cost of delivered power by reducing transmission congestion.[61] The Commission established a rebuttable presumption that a project is eligible for incentives under section 219 if it: (1) results from a fair and open regional planning process that considers and evaluates projects for reliability and/or congestion and is found to be acceptable to the Commission; or (2) has received construction approval from an appropriate state commission or state siting authority.[62] The Commission also stated that it will consider incentive requests for projects that are still undergoing consideration in a regional planning process, but may make any requested incentive rate treatment contingent on the project being approved under the regional planning process.[63]

57. We find that the Project does qualify for the rebuttable presumption because it is the product of the regional planning process in New England, which the Commission has approved as a fair and open planning process. As a part of the New England regional planning process, ISO-NE evaluates the reliability and congestion benefits of a proposed transmission project. Accordingly, because the Project is included in the ISO-NE Regional System Plan as a reliability upgrade,[64] it is entitled to the rebuttable presumption that it satisfies the requirements of section 219.

4. Obligation to Build

a. Protest

58. The Mass. AG argues the ROE incentives requested will not increase the likelihood that the Springfield Component will be constructed, but will instead only raise the cost of the project to ratepayers. Further, the Mass. AG states Western Mass. Electric has obligated itself to develop and construct the

[61] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 57-58.

[62] *Id*. P 57-58. In Order No. 679-A, the Commission clarified the operation of this rebuttable presumption by noting that the authorities and/or processes on which it is based (i.e., a regional planning process, a state commission, or siting authority) must, in fact, consider whether the project ensures reliability or reduces the cost of delivered power by reducing congestion. Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 49.

[63] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at n.39.

[64] Transmittal Letter at 7.

Springfield Component upgrades to provide the remedies contemplated under the Western Mass. Electric Settlement.[65] Mass. AG contends that Western Mass. Electric's investors do not have the right to forego these upgrades, which undercuts Applicants' assertion the projects will face greater internal scrutiny and internal competition for financing without the requested incentives.

59. The Joint Protesters, MMWEC, and Chicopee and South Hadley contend that the Project should not be eligible for incentives because the Applicants have a contractual obligation to build new transmission included in ISO-NE's Regional System Plan, subject to approval by the relevant state siting authorities. MMWEC states that Applicants already receive a 50 basis point ROE adder for its membership in ISO-NE and contends that it is unreasonable to require customers to pay incentives that compel the performance of Applicants' contractual obligation. MMWEC acknowledges that the Commission rejected this same argument in *Northeast Utilities*,[66] where it expressed concern that accepting such a narrow interpretation of the Commission's authority would prevent it from granting an ROE transmission investment incentive under any circumstance. MMWEC states that it disagrees with the Commission's decision in *Northeast Utilities* because refusing incentives in New England, where transmission owners are contractually obligated to build, would not hinder the Commission in granting incentives in regions of the country where transmission owners have not voluntarily assumed the obligation to build.

b. Commission Determination

60. We reject MMWEC's and Mass. AG's arguments as a collateral attack on *Northeast Utilities*. In *Northeast Utilities*, the Commission rejected the assertion that projects in ISO-NE's Regional System Plan are ineligible for incentives merely because the transmission owner may have a contractual obligation to build them. The Commission found that this argument was a narrow interpretation of Order No. 679 and that accepting it would deny the Commission the ability to exercise the authority it was expressly granted under section 219.[67] As MMWEC

[65] Settlement Agreement, section 2.2, D.T.E. 06-55 (Massachusetts Department of Telecommunications and Energy, October 19, 2006) (Western Mass. Electric Settlement).

[66] *Northeast Utilities Service Co.*, 124 FERC ¶ 61,044, at P 89 (2008) (*Northeast Utilities*).

[67] *Id.*

itself acknowledges, it makes the same argument in this proceeding that the Commission rejected in *Northeast Utilities*. Finally, Order No. 679-A explicitly states that an obligation to build does not preclude eligibility for incentives, although such obligations "may have a bearing on our nexus evaluation of individual applications."[68] MMWEC's narrow interpretation of Order No. 679 would deny the Commission the ability to exercise the authority that Congress expressly granted the Commission in FPA section 219.

5. Incentives and the Commission's Nexus Test

a. Protest

61. Chicopee and South Hadley state that the requested incentives, if granted, would upset the balance of consumer and investor interests by imposing on ratepayers unjust and unreasonable rates. The Mass. AG argues that Western Mass. Electric has not demonstrated that treating all of the Project upgrades as a group is appropriate for determining whether the proposed incentives are tailored to the Project's risks because the different components of the project are independent of each other. NRG asserts the risks identified do not exceed normal business risk and transmission providers already have the benefit of cost-socialization and the safety net of cost-of-service recovery.[69]

62. NRG argues that the best way to support efficient, competitive wholesale markets is through exploring all options, including generation and demand-side alternatives. When considering transmission upgrades such alternatives are disadvantaged, according to NRG, even without the incentive ROE because "transmission alone does not provide for resource adequacy or complete operational reliability."[70] NRG prefers that the incentives be rejected in favor of a cost-benefit analysis of alternatives to the transmission lines. Incentives should only then be considered to stimulate construction. Establishing the "nexus" requires an analysis of the benefits and risks of the proposed project. NRG points to a December 2006 ISO-NE Presentation about the Southern New England Transmission Reinforcement, concluding new generation in specific locations could "defer the need for" two of the four transmission segments of the Project

[68] *Id.*; Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 122.

[69] NRG Protest at 7.

[70] *Id.* at 3.

(specifically, the Interstate and Connecticut Components).[71] NRG also argues that Applicants provide no analysis of projected congestion costs savings or decreased energy prices of the four segments in the Project.[72]

63. Joint Protesters state that owning transmission offers low business risks, providing a stable source of cash flow to the consolidated entity. Recovery of prudently incurred costs on abandoned construction coupled with the inclusion of 100 percent CWIP in the rate base should insulate the Applicants, their subsidiaries, lenders, and equity investors from the investment risks associated with the Project. Joint Protesters argue the Applicants did not show that a transmission project offering an 11.64 percent ROE with the recovery of investment under a formula rate cannot attract capital or provide the needed reassurance to investors. The Applicants also fail to demonstrate a return 150 basis points above the base ROE is the only return figure that could provide the necessary capital, according to MMWEC.

64. Joint Protesters dispute the Applicants' interpretation of financial reports. MMWEC argues the financial reports cited by the Applicants express concern over the size of the cost burden *during* construction – an issue more appropriately addressed by the CWIP and abandonment incentives. MMWEC points to the fact that Standard & Poor's described the overall business profile of Northeast Utilities as excellent.

b. Commission Determination

65. In addition to satisfying the section 219 requirement of ensuring reliability or reducing the cost of delivered power by reducing congestion, an applicant must demonstrate that there is a nexus between the incentive sought and the investment being made. In Order No. 679-A, the Commission clarified that the nexus test is met when an applicant demonstrates that the total package of incentives requested is "tailored to address the demonstrable risks or challenges faced by the applicant."[73]

66. As part of the evaluation of whether the incentives requested are tailored to address the demonstrable risks or challenges faced by the applicant, the

[71] *Id*. at 4.

[72] *Id*. at 6.

[73] Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 40.

Commission has found the question of whether a project is "routine" to be particularly probative. In *BG&E*, the Commission provided guidance on the factors that it will consider when determining whether a project is routine. The Commission stated that it will consider all relevant factors presented by the applicant, including evidence on: (1) the scope of the project (e.g., dollar investment, increase in transfer capability, involvement of multiple entities or jurisdictions, size, effect on region); (2) the effect of the project (e.g., improving reliability or reducing congestion costs); and (3) the challenges or risks faced by the project (e.g., siting, internal competition for financing with other projects, long lead times, regulatory and political risks, specific financing challenges, other impediments).[74] The Commission also explained that when an applicant has adequately demonstrated that the project for which it requests an incentive is not routine, that applicant has, for purposes of the nexus test, shown that the project faces risks and challenges that merit an incentive.[75]

67. We find that the Project's size and scope indicate that it is not a routine transmission investment. It is a complex addition to the New England 345-kV transmission system crossing three states, Connecticut, Rhode Island, and Massachusetts, and represents a large-scale, regional transmission solution involving improvements to the Northeast Utilities' and National Grid's transmission systems. Applicants have presented evidence on the Project's scope, effect, and risks. The Project has an estimated cost of $2.1 billion. In dollar terms, the Project is among the largest transmission infrastructure projects that the Applicants have pursued. Further, the $2.1 billion total project cost and the length of time to get approvals or place the line in service justify the need for the incentives to maintain the credit ratings.

68. Additionally, the Project's effect is to increase the reliability and capacity for power transfers across the New England power grid, as well as address multiple reliability issues for New England as a whole. It will upgrade and expand the region's 345-kV backbone transmission, and will ensure that the southern New England grid is reliable and complies with the reliability standards of North American Electric Reliability Corporation, Northeast Power Coordinating Council, and ISO-NE.

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[74] *Baltimore Gas & Electric Co.*, 120 FERC ¶ 61,084, at P 52-55 (2007) (*BG&E)*.

[75] *Id*. P 54.

69. Applicants face substantial challenges and risks - financial, regulatory, environmental, and siting as well as facing internal competition for financing with other projects. Based on this evidence, we find that Applicants have adequately demonstrated that the Project is not routine, and thus, have sufficiently demonstrated a nexus between the incentives sought and the investment being made. For example, Applicants will encounter siting challenges because the Project runs through three different states. It will need to undergo a comprehensive siting process before the Connecticut Siting Council, the Massachusetts Energy Facilities Siting Board, and the Rhode Island Energy Facility Siting Board, which will consider numerous factors, including alternatives to each of the projects (such as route alternatives, potential environmental and social issues, electric and magnetic field issues, engineering designs, costs, etc.). Further, prior to actually submitting siting applications, Applicants must engage in a municipal consultation process that is designed to obtain input and comments from the public and local government representatives in each of the Connecticut, Massachusetts and Rhode Island municipalities in which the preferred or alternative routes of the proposed Project are located. In addition to the siting approvals, the Project will require numerous other permits at the federal, state and local level.

70. Chicopee and South Hadley argue that the requested incentives would impose on ratepayers unjust and unreasonable rates because they are excessive considering they include ROE as well as CWIP and abandoned plant. NRG argues that the Applicants ought to have performed a cost-benefit analysis, including that of non-transmission alternatives. This is contrary to Order Nos. 679 and 679-A in which the Commission held that a cost-benefit analysis is not required.[76] Additionally, Order No. 679 does not require applicants to perform a comparative cost-benefit of non-transmission alternatives in order to be eligible for incentive rate treatment. The fact that the Project has been reviewed and approved under the ISO-NE's regional planning process entitles the Applicants to a rebuttable presumption that the project ensures reliability or reduces transmission congestion, or both.[77] Our grant of transmission incentives is not intended to preclude the selection of non-transmission alternatives. It is merely intended to provide assurance that if the project does go forward, it will be afforded these incentives.

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[76] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 65; Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 35-40.

[77] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 58.

71. Finally, Joint Protesters argue that the Commission should find that Applicants face little actual financial risk and thus have failed to demonstrate that there is a nexus between the incentives being sought and the investment being made. We reject this argument as contrary to the holding in *BG&E*. In *BG&E*, the Commission explained that when an applicant has adequately demonstrated that the project for which it requests an incentive is not routine, that applicant has, for purposes of the nexus test, shown that the project faces risks and challenges that merit an incentive.[78] As we have explained, Applicants have adequately demonstrated that its Project is not routine.

6. Specific Incentives and Total Package of Incentives

a. Protest

i. ROE Incentive

72. Chicopee and South Hadley point out that an investment in a relatively low-risk, transmission-only entity with an 11.64 percent ROE may be an attractive option for many investors. Also, the Joint Protesters contend that the 74 basis point adder included in the 11.64 percent ROE granted by Order No. 489 reflect a set of conditions that no longer exists, meaning the additional adder is no longer justified. The effects of recent moves in the equity market mean the 13.14 percent ROE is inflated even beyond the 150 basis point "incentive" adder due to falling bond yields and lower expectation of ROE in the common equity markets as a whole since the issuance of Opinion No. 489. The Joint Protesters state the 13.14 percent ROE is equivalent to a 260 to 274 basis point adder, and represents a true incremental cost to New England ratepayers over a 30-year project lifetime of between $700 and $800 million. They state the incremental cost to the ratepayers of the 150 basis point adder alone is between $370 and $400 million over an estimated 30-year lifetime of the Project.

73. Further, Chicopee and South Hadley take issue with the Applicants' observation that its requested ROE of 13.14 percent is lower than the 14.3 percent ROE granted in *Potomac-Appalachian Transmission Highline, L.L.C.*,[79] noting all incentive cases should be determined on a case-by-case basis. They note in *PATH* a discounted cash flow (DCF) analysis returned a zone of reasonable returns with a midpoint of 11.34 percent, nearly 100 basis points above the midpoint of 10.4 percent in the instant case.

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[78] *BG&E*, 120 FERC ¶ 61,084 at P 54.

[79] 122 FERC ¶ 61,188, at P 104 (2008) (*PATH)*.

74. The Joint Protesters explain that conditions have changed in the bond market since the Commission issued Order No. 489 in August 2006. The average monthly yield on 10-year U.S. Treasury bonds for the six-month period from April 2008 to September 2008 was 3.88 percent. Therefore, they claim an updated ROE with a downward adjustment of 110 basis points might be more appropriate. For support, they point out that currently the expected ROE on the Standard and Poor's 500 has fallen by 124 basis points.

75. The Joint Protesters contend the Petitioners fail to demonstrate that the adder is within the zone of reasonableness because the range is based on outdated data, and the Applicants do not establish "the continued reasonableness" of a zone with a high end of 13.5 percent or a midpoint of 10.4 percent.[80] They argue some of the group members do not face risks representative of electric transmission companies in the northeast. This illustrates a threshold flaw in the proxy group used to create the baseline ROE proposal. They further argue the Commission should recognize the significant risk differentials between the proxy companies and the Applicants by setting the ROE at the lower end of the proxy group range of returns. A second reason for inaccuracy is the high estimated average cost of equity for the Standard and Poor's 500, a proxy for the equity market as a whole, resulting in an average expected ROE of 13.0 percent. The Joint Protesters assert the base ROE should be reduced to a midpoint of 10.05 percent resulting in a zone of reasonableness of 8.3 percent to 12.8 percent.[81]

ii. CWIP

76. No party protests the Applicants' request to include 100 percent of prudently-incurred CWIP in rate base. However, if the Commission grants the CWIP incentive, the Mass. AG asks the Commission to clarify that the cost allocation of the CWIP recovery will be in the same manner that the cost of the projects would have been allocated upon completion. The Mass. AG states that this would ensure that (1) Local Network Service customers are not subsidizing CWIP costs that should be regionalized; and (2) Regional Network Service customers are not subsidizing CWIP costs that should be localized.[82]

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[80] The Joint Protesters Protest at 11.

[81] *Id.* at 13.

[82] Mass. AG Protest at 9.

iii. Abandonment

77. Chicopee and South Hadley argue the Applicants should be held to the abandoned plant protection agreed to in Schedule 3.09(a) of the TOA since they have not shown the TOA protections are inapplicable. MMWEC states the Applicants appear to be using the instant case and the Order No.679 incentives as an opportunity to do what they are already obligated to do under the TOA, that is build transmission necessary and appropriate for reliability.[83] MMWEC argues Applicants should attempt to make the *Mobile-Sierra*[84] showing that is necessary to justify a unilateral modification of these incentives instead of seeking the same kinds of incentives it has through the TOA.

iv. Total Package of Incentives

78. Joint Protesters argue that the requested ROE incentive compensates the Applicants for risks largely eliminated if they are also granted the CWIP and abandonment incentives, similar to the Commission's finding in *Southern California Edison Co.*[85] Thus, Protesters contend that the 150 basis point adder is excessive and ask the Commission to reduce the adder to reflect the extent to which risk has been mitigated by the other two incentives. MMWEC notes that not all returns within the range of reasonableness are necessarily just and reasonable.

79. Protesters state that Applicants will recover the cost of the Project through formula rates, which further reduce their risk. In addition, Joint Protesters state that an up-front ROE determination serves as a de facto incentive reducing regulatory risk.

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[83] *See* ISO-NE TOA at Schedule 3.09(a).

[84] *See United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956); *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Mobile-Sierra*); ISO-NE TOA at section 11.04(c).

[85] 121 FERC ¶ 61,168, at P 143 (2007).

b. Commission Determination

i. ROE Incentive

80. We find that Applicants have demonstrated that the Project is non-routine and that the significant risks and challenges faced by the Project warrant the granting of an ROE incentive. Applicants face significant siting risks because the Project is expected to be built along over 300 miles of transmission corridors. The new 345-kV lines and upgraded 115-kV lines cover three states and require a joint siting effort of two utilities. Applicants face regulatory risks because the Project must be approved by at least fifteen state agencies, three federal agencies, and numerous local municipalities. Applicants also face significant financial risks, given the Project's estimated $2.1 billion cost. Our decision to authorize an ROE incentive is consistent with section 219's goal of encouraging transmission investment.

81. Although Applicants have sufficiently demonstrated that the Project faces risks and challenges that warrant an ROE incentive, we agree with Chicopee and South Hadley and the Joint Protesters that a 150 basis point adder is not justified in this case. We find that Applicants' overall risk is reduced by our decision, discussed below, to authorize the requested CWIP and abandonment incentives.[86] Accordingly, based on the facts of this case, we authorize a 125 basis point ROE incentive adder for the Project, to be bound by the upper end of the zone of reasonableness established in Opinion No. 489. The Opinion No. 489 Rehearing Order modified the high-end implied cost of equity and the midpoint ROE for the New England Transmission Owners.[87] As a result, the zone of reasonableness for the New England Transmission Owners is 7.3 percent to 13.5 percent, with a midpoint ROE of 10.4 percent.[88]

82. The "going-forward" ROE for New England Transmission Owners is 11.64 percent, including the 50 basis point incentive for RTO participation and the 74 basis point adjustment reflecting updated bond data, applicable as of November 1, 2006 (10.4 + 0.5 + 0.74).[89] Our granting of a 125 basis point adder, in conjunction

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[86] *See e.g.*, *Pepco*, 124 FERC ¶ 61,176; *Virginia Electric Power Co.*, 124 FERC ¶ 61,207 (2008) (*VEPCO*).

[87] Opinion No. 489 Rehearing Order, 122 FERC ¶ 61,265 at P 9-13.

[88] *Central Maine*, 125 FERC ¶ 61,079 at P 72.

[89] *Id.* P 73.

with the 11.64 percent base level ROE as determined by the Opinion No. 489 Rehearing Order, results in a 12.89 percent ROE (10.4 + 0.5 + 0.74 + 1.25), which falls within the upper range of the zone of reasonableness.

83. We reject the Joint Protesters claim that a recent decline in 10-year U.S. Treasury bond yields makes the 74-basis point upwards adjustment to the current New England Transmission Owners' midpoint ROE inappropriate under current market conditions.[90] As we stated in *Central Maine*,[91] the 74 basis point bond adjustment applies to the midpoint of the zone of reasonableness. Joint Protesters have not demonstrated that this decline in Treasury bond rates correlates to a reduction in corporate borrowing costs or the cost of capital, based on current market conditions.

84. We note the Commission recently performed a similar DCF analysis based on the Opinion No. 489 methodology in *Pepco Holdings, Inc.*[92] In *PHI*, Pepco Holdings, Inc. (Pepco) began with a similar group of fifteen northeast transmission owners[93] for its proxy group before additional screens were applied and reduced the proxy group. Updated data for the six month period ending January 2008 was used for the Pepco proxy group. Northeast Utilities and Pepco are both rated BBB by Standard & Poor's, which results in companies rated below BBB- or above BBB+ being screened out of the proxy group.[94] Pepco's proxy group thus provides a reasonable comparison for determining the zone of reasonable returns for Northeast Utilities. In *PHI*, the zone of reasonableness was determined to be

[90] Kivela Affidavit at P 8-15.

[91] *Central Maine*, 125 FERC ¶ 61,079 at P 73.

[92] *Pepco Holdings, Inc.*, 124 FERC ¶ 61,176 (2008) *(PHI)*.

[93] These fifteen transmission owners all belong to ISO New England, the New York Independent System Operator, Inc., or PJM Interconnection, L.L.C.

[94] In addition to screening the utilities based upon their corporate credit ratings, the Pepco proxy group also excludes: (1) utilities that are not currently paying cash dividends; (2) utilities that have announced a merger during the six-month period used to calculate the dividend yields; (3) utilities primarily operating as natural gas companies; (4) utilities that do not have both an IBES (International Brokers Estimation System) growth rate and *Value Line* data; and (5) utilities with unsustainably high growth rates.

7.0 percent to 15.9 percent,[95] so the 12.89 percent ROE granted to Northeast Utilities falls well within this range. Therefore, the zone of reasonableness approved in *PHI* demonstrates that the continued use of the New England Transmission Owners' zone of reasonableness of 7.3 percent to 13.5 percent is appropriate. The Commission has recently performed a similar analysis based on the Opinion No. 489 methodology for a utility rated BBB+ by Standard and Poor's similar to National Grid's parent in *VEPCO*.[96] In *VEPCO*, using updated data for the six month period ending May 2008, the zone of reasonableness was determined to be 9.46 percent to 14.4 percent.[97]

85. Further, we would note that the Applicants submitted a similar DCF analysis based on the Opinion No. 489 methodology, using updated data for the six month period ending July 2008. The zone of reasonableness was determined to be 8.3 percent to 15.7 percent whether or not the corporate credit ratings screen was applied, so this result applied equally to both Northeast Utilities and National Grid even though they had differing corporate credit ratings. Based upon all three of these analyses, the Commission concludes that the 13.5 percent high end ROE remains reasonable and that the 12.89 percent ROE granted to Applicants remains within the zone of reasonableness.

86. Finally, we are not persuaded to accept the Joint Protesters' arguments on the composition of the Applicants' proxy group, such as excluding utilities that own generation[98] and using the 13.0 percent average ROE from a Standard and Poor's 500 proxy group to limit the high end ROE of the Applicants.[99] These adjustments to the proxy group would result in an adjusted zone of reasonableness of 8.3 percent to 12.8 percent. The elimination of generation-owning utilities from a proxy group is inconsistent with Commission precedent. [100] In addition, the Commission does not believe that it is appropriate to eliminate high-end ROEs from a proxy group if they exceed the average ROE of a proxy group based upon

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[95] *PHI*, 124 FERC ¶ 61,176 at P 114-116.

[96] *Virginia Electric & Power Co.*, 124 FERC ¶ 61,207 (2008) (*VEPCO*).

[97] *Id.* P 120.

[98] Kivela Affidavit at P 31-41.

[99] *Id.* P 42-50.

[100] Opinion No. 489, 117 FERC ¶ 61,129 at P 38.

the Standard and Poor's 500. It is not consistent with Commission precedent to cap the upper end of the zone of reasonableness with the average ROE of another proxy group.

ii. CWIP

87. In Order No. 679, the Commission established a policy that allows utilities to include, where appropriate, 100 percent of prudently-incurred transmission-related CWIP in rate base.[101] The Commission stated that this rate treatment will further the goals of section 219 by providing up-front regulatory certainty, rate stability, and improved cash flow, reducing the pressures on an applicant's finances caused by investing in transmission projects.[102]

88. We find that the Applicants have shown a nexus between the proposed CWIP incentive and its investment in the Project. Connecticut Light's and Western Mass. Electric's portion of the project for which they are seeking incentives, which will cost approximately $1.049 billion, is 131 percent of their net transmission plant in service as of the end of 2007, 79 percent of their projected net transmission plant in service for 2008, and 61 percent of their projected net transmission plant in service for 2009. In addition, Connecticut Light's and Western Mass. Electric's investments represent 91 percent of their total transmission capital expenditures for the 2003-2007 period.[103] Similarly, National Grid's share of the Project will exceed its total annual transmission construction costs over the six-year period ending March 31, 2008. The Project will also represent the largest investment for National Grid in recent years.[104] The Applicants further demonstrate that the inclusion of 100 percent CWIP in rate base for the period 2008-2013 will provide Connecticut Light and Western Mass. Electric with an estimated $137 million more during the construction period than if not granted this incentive, as well as an interest expense savings of $4.6 million during the same period.[105]

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[101] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 29, 117.

[102] *Id.* P 115.

[103] Exhibit No. NU/NG-200 at 7.

[104] Joint Transmittal Letter at 16-17.

[105] *See* Exhibit No. NU/NG-200 at 22. *See also* Exhibit No. NU/NG-208.

89. Consistent with Order No. 679, we find that authorizing 100 percent of CWIP will enhance the Applicants' cash flow, reduce interest expense, assist with financing, and improve the coverage ratios used by rating agencies to determine the Applicants' credit quality by replacing non-cash AFUDC with cash earnings. This, in turn, will reduce the risk of a downgrade in their debt ratings. Considering the size of the investment in the Project, we find that authorization of the CWIP incentive is appropriate. We also find that allowing the Applicants to recover 100 percent of CWIP in their rate base will result in better rate stability for customers. As we have explained in prior orders,[106] when certain large-scale transmission projects come on-line, there is a risk that consumers may experience "rate shock" if CWIP is not permitted in rate base. By allowing 100 percent CWIP in rate base, the rate impact of the Project can be spread over the entire construction period and will help consumers avoid a return on and of capitalized AFUDC.[107]

90. Pursuant to Order No. 679 and 18 C.F.R. § 35.25, a company must propose accounting procedures that ensure that customers will not be charged for both capitalized AFUDC and corresponding amounts of CWIP in rate base. The Commission finds that the Applicants' proposed accounting procedures in Exhibits NU/NG 400-403 and NU/NG 500-501 of their filing sufficiently demonstrate that they have accounting procedures and internal controls in place to prevent recovery of AFUDC to the extent it is allowed to include CWIP in rate base.

91. Further, to promote comparability of financial information between entities,[108] the Commission has required a specific accounting treatment or the use of footnote disclosures to recognize the economic effects of having CWIP in rate base. Northeast Utilities and New England Power have provided specific accounting treatments that satisfy the Commission's desire for the comparability of financial information. Narragansett has not proposed any specific accounting treatments because it chose not to accrue for AFUDC. However, Narragansett has

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[106] *See e.g.*, *American Electric Power Service Corp.*, 116 FERC ¶ 61,059, at P 59 (2006), *order on reh'g*, 118 FERC ¶ 61,041, at P 27 (2007); *PPL*, 123 FERC ¶ 61,068 at P 40-P 43.

[107] *Id.*

[108] The Commission's Uniform System of Accounts (USofA), Electric Plant Instruction No. 3, requires AFUDC to be capitalized as a component cost of construction and depreciated over the service life of the asset.

not proposed to provide footnote disclosures to recognize the economic effects of having CWIP in rate base. The Commission therefore directs Narragansett to provide footnote disclosures in the notes to the financial statements of their annual FERC Form No. 1 and their quarterly FERC Form No. 3-Q which (1) fully explain the impact of the CWIP in rate base; (2) include details of AFUDC not capitalized because of CWIP in rate base for the current year, the previous two years, and the sum of all years; and (3) include a partial balance sheet consisting of the Assets and Other Debits section of the balance sheet to include the amounts of AFUDC not capitalized because of the inclusion of CWIP in rate base.

92. Further, to address the Mass. AG concerns, we clarify that the cost allocation of the CWIP recovery will be done in the same manner that the cost of the projects would have been allocated upon completion.

iii. Abandonment

93. In Order No. 679, the Commission found that abandonment is an effective means to encourage transmission development by reducing the risk of non-recovery of costs.[109] We find that Applicants have demonstrated a nexus between the recovery of prudently incurred costs associated with abandoned transmission projects and its planned investment. Thus, we will grant Applicants' request for recovery of 100 percent of prudently-incurred costs associated with abandonment, provided that the abandonment is a result of factors beyond the Applicants' control, which must be demonstrated in any subsequent section 205 filings for recovery of abandoned plant.[110]

94. We find that this incentive will be an effective means to encourage the Project's completion. For example, in addition to the challenges presented by its scope and size, the Project requires approvals from multiple municipalities within Connecticut, Rhode Island and Massachusetts, state siting authorities, and various federal approvals. Moreover, the Project risks cancellation should it fail to receive state siting authority. These factors introduce a significant element of risk; authorizing abandonment will help ameliorate this risk by providing Applicants with some degree of certainty as it moves forward. Order No. 679's abandonment incentives are broader in scope than those given in the ISO-NE TOA.

95. We will not determine the justness and reasonableness of Applicants' abandoned plant recovery, if any, until Applicants seek such recovery in a section

[109] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 163.

[110] *Id*. P 165-66.

205 filing. Order No. 679 specifically reserves the prudence determination for the later section 205 filing that every utility is required to make if it seeks abandonment recovery.[111] At this stage of the proceeding, we grant this incentive, subject to Applicants making the appropriate demonstration in a future section 205 filing.

96. Finally, we reject MMWEC's and Chicopee and South Hadley's arguments that the Applicants should be held to the abandoned plant protections in the TOA. Applicants seek abandonment protections afforded under Order No. 679, and we conclude that they are within their rights to make such a request regardless of the abandonment protections afforded by the TOA. The standard set forth in Order No. 679 is whether abandonment "is outside the control of management,"[112] and not whether other abandonment protections are applicable. Therefore, we do not address the issue of how to interpret or apply any abandonment protection that may be afforded by the TOA.

iv. Total Package of Incentives

97. The total package of incentives requested must be tailored to address the demonstrable risks or challenges faced by the applicant. This examination is fact-specific and requires the Commission to review each application on a case-by-case basis. Consistent with Order No. 679, the Commission has, in prior cases, approved multiple rate incentives for particular projects as long as each incentive satisfies the nexus test. [113]

98. We find that Applicants have shown that the total package of incentives is tailored to address the demonstrable risks and challenges faced by the Project.[114]

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[111] *Id*.

[112] *Id*. P 163.

[113] *See id*. P 55; *see also, e.g.*, *Allegheny Energy, Inc.*, 116 FERC ¶ 61,058, at P 60, 122 (2006) (approving ROE at the upper end of the zone of reasonableness and 100 percent abandoned plant recovery); *Duquesne*, 118 FERC ¶ 61,087 at P 55 (granting an enhanced ROE, 100 percent CWIP, and 100 percent abandoned plant recovery); *PPL*, 123 FERC ¶ 61,068 at P 39, 42, 46 (approving ROE at the upper end of the zone of reasonableness, 100 percent CWIP, and 100 percent abandoned plant recovery).

[114] Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 21, 27.

As we have stated, Applicants face significant risks and challenges in constructing the Project; we find that authorizing the ROE, CWIP, and abandonment incentives will encourage investors to invest in the Project despite these risks.

99. Order No. 679-A provided that if some of the incentives in the total package of requested incentives reduce a project's risk, the Commission will take that fact into account when considering any request for an enhanced ROE.[115] While the Applicants' requested incentives fall within the scope of incentives outlined in Order No. 679, we agree with Joint Protesters to the extent that granting the CWIP and abandonment incentives reduces the overall risk. The ability to include CWIP in rate base will result in an infusion of cash and reduced financial risk during construction. Moreover, an entity allowed to include 100 percent CWIP in rate base is not required to refund the prudently-incurred costs collected.[116] Similarly, abandonment ensures that investors will recover a return on an investment, thereby further reducing financial risk associated with these investments.[117]

100. Considering the total package of incentives requested, we find that a 125 basis point ROE adder, lowered from the requested 150 basis points, is appropriate.[118] We are not persuaded by Joint Protesters' argument that having a

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[115] *Id*. P 8.

[116] *Id*. P 116 ("[W]here an applicant has satisfied our nexus requirement and has been granted authority to recover CWIP or abandoned plant, and subsequently the applicant's project is unable to obtain state or federal siting authority (and thus no showing is made with respect to ensuring reliability or reducing the cost of delivered power by reducing congestion because the applicant was relying upon those processes) we would not require refunds for the costs already prudently-incurred by the applicant. To require refunds in such circumstances would be contrary to our long-standing policy, which permits recovery of all prudently-incurred costs.") (original footnote omitted).

[117] *See* Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 167 ("[A] utility that receives approval to recover abandoned plant in rate base would likely face lower risk and thus may warrant a lower ROE than would otherwise be the case without this assurance.").

[118] *See Southern California Edison Co.*, 121 FERC ¶ 61,168, at P 143 (2007); *reh'g denied*, 123 FERC ¶ 61,293 (2008).

formula rate and/or receiving an up-front ROE determination necessarily warrants a lower ROE in this case. The Commission believes that the scope, effects, risks and challenges of the Project are commensurate with a 125 basis point ROE adder.

The Commission orders:

(A) The transmission incentives are hereby granted, as modified herein, as discussed in the body of this order.

(B) The proposed tariff revisions are hereby accepted for filing, to become effective on November 18, 2008, as discussed in the body of this order.

By the Commission. Commissioner Kelly concurring in part and dissenting in part with a separate statement to be issued at a later date. Commissioner Wellinghoff dissenting in part with a separate statement to be issued at a later date.

(S E A L)

Kimberly D. Bose,
Secretary.