

125 FERC ¶ 61,028  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

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

Duquesne Light Company

Docket Nos. ER08-1402-000

ORDER GRANTING TRANSMISSION RATE INCENTIVES

(Issued October 10, 2008)

1. On August 14, 2008, Duquesne Light Company (Duquesne) filed revised tariff sheets pursuant to section 205 of the Federal Power Act (FPA),<sup>1</sup> to the Open Access Transmission Tariff (OATT) administered by PJM Interconnection, L.L.C. (PJM). The revised tariff sheets reflect two Order No. 679<sup>2</sup> transmission rate incentives for the Brady Project, a PJM Regional Transmission Expansion Plan (RTEP) project which includes high-voltage transmission facilities in the Pittsburgh, Pennsylvania area. Specifically, Duquesne requests a return on equity (ROE) incentive adder of 150-basis points and recovery of 100 percent of its costs for construction work in progress (CWIP). For the reasons discussed below, the Commission will grant the requested incentives and accept the revised tariff sheets, effective October 13, 2008, as requested.

**I. Background**

2. Duquesne is a wholly-owned subsidiary of Duquesne Light Holdings, Inc., a Pennsylvania corporation and intrastate holding company. Duquesne is engaged in the purchase, transmission, and distribution of electric energy to approximately 587,000 customers in a service territory of approximately 800 square miles in southwestern Pennsylvania. Duquesne presently owns no generating assets.

3. On September 29, 2006, Duquesne made two companion filings at the Commission (1) to convert from a stated rate to a formula rate and (2) to request transmission incentives for the Duquesne Transmission Enhancement Plan (DTEP). By orders issued on February 6, 2007, and May 9, 2008, the Commission approved the

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<sup>1</sup> 16 U.S.C. § 824d (2006).

<sup>2</sup> *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).

formula rate and the following incentives: (1) a 50-basis point ROE adder for continued membership in PJM; (2) a 100-basis point transmission incentive adder for the DTEP; (3) 100 percent recovery of transmission-related CWIP costs for the DTEP in rate base; and (4) 100 percent recovery of abandonment costs for the DTEP, if the abandonment is due to reasons beyond the control of Duquesne's management.<sup>3</sup> The Commission also approved an uncontested settlement which established a base ROE of 11.4 percent, inclusive of the 50 basis points for continued membership in PJM, and an ROE of 11.9 percent for the DTEP.<sup>4</sup>

4. Under the DTEP, Duquesne planned to construct a new high-voltage transmission line to enhance the reliability of the 138-kV and 345-kV transmission service to Pittsburgh and surrounding areas. Duquesne also planned to increase the carrying capacity of two existing underground 345-kV lines by using a state-of-the-art forced cooling technology between its Brunot Island and Arsenal substations. Further, the DTEP involved the upgrading of certain 69-kV facilities to 138-kV on the northeastern and western portions of its 138-kV systems. The DTEP was originally estimated to cost \$184 million, which was roughly 76 percent of Duquesne's then current net transmission plant in service.<sup>5</sup> In the instant application, Duquesne puts the cost of the DTEP at \$220 million.

5. Duquesne's transmission facilities were integrated into PJM on January 1, 2005. However, Duquesne is in the process of withdrawing from PJM to join the Midwest Independent Transmission system Operator, Inc. (MISO).<sup>6</sup> In orders issued on January 17, 2008 and September 3, 2008, the Commission conditionally approved Duquesne's withdrawal from PJM.<sup>7</sup> On July 25, 2008 in Docket No. ER08-1309-000, Duquesne and MISO filed to establish formula rates for Duquesne under MISO's OATT.

6. Duquesne states that its transition to MISO will not impact the Brady Project. It further states that it has committed to complete all of the reliability-based transmission enhancements approved by PJM. In addition, Duquesne states that MISO has assured

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<sup>3</sup> *Duquesne Light Co.*, 118 FERC ¶ 61,087 (2007) (*Duquesne*).

<sup>4</sup> *Duquesne Light Co.*, 123 FERC ¶ 61,139 (2008) (*Order Accepting Uncontested Settlement*).

<sup>5</sup> *Duquesne*, 118 FERC ¶ 61,087 at P 52.

<sup>6</sup> *Midwest Independent Transmission System Operator, Inc. and Duquesne Light Company*, 124 FERC ¶ 61,219 (2008) (*MISO/Duquesne Order*).

<sup>7</sup> *Duquesne Light Co.*, 122 FERC ¶ 61,039, *clarified*, 123 FERC ¶ 61,060 (2008) (January 17, 2008 Order); *MISO/Duquesne Order*, 124 FERC ¶ 61,219 at P 10.

Duquesne that it will accept Duquesne's transmission projects approved through the PJM RTEP process without further analysis.

## **II. Proposal**

### **A. The Brady Project**

7. As required by PJM's 2007 RTEP, Duquesne proposes to construct a major new substation and related 345-kV- and 138-kV-transmission lines, including extensive pipe-type underground cables, to maintain reliable service to Pittsburgh and the surrounding tri-state area. The Brady Project will complement the DTEP by completing a 345-kV-transmission ring around Pittsburgh. The Brady Project is expected to be in service by June 2012 and to cost approximately \$291 million.

8. The Brady Project has three main components. First, the project includes the construction of a new 345/138-kV-downtown substation called the Brady substation. Second, the project includes the installation of a new underground 345-kV line between the Brunot Island and Carson substations, which will run through the newly-constructed Brady substation. This new line will complete the 345-kV loop around Pittsburgh and enhance reliability in the region by relieving heavy loading on the underground 345-kV lines between the Brunot Island and Arsenal substations as well as providing additional transmission capacity to Pittsburgh. Third, Duquesne will replace the Oakland-Carson Z-86 138-kV cable with large, higher-rated 138-kV cable which will also be routed and looped through the Brady substation.<sup>8</sup> Duquesne states that the \$291 million cost of the Brady Project is a massive financial burden considering that Duquesne's transmission plant in service as of December 31, 2007 was \$309.7 million.

9. Duquesne states that the Brady Project is a non-routine system expansion which involves the construction of substation facilities and high-voltage transmission lines in a densely populated urban setting. Duquesne further states that coordinating the construction of the Brady Project with the DTEP is a complex logistical undertaking that increases the financial burden and risk to completing both projects in a timely manner.

### **B. Incentive for CWIP**

10. Duquesne requests recovery of 100 percent of CWIP costs for the Brady Project incurred prior to its in-service date. Once Duquesne transfers to MISO, it will reflect the CWIP costs associated with the Brady Project as a line item in its formula rate under MISO's OATT. For the Brady Project, Duquesne agrees to abide by the accounting procedures accepted by the Commission for the DTEP to ensure that Duquesne's

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<sup>8</sup> Duquesne's filing, Exhibit No. DLC-1 at 6.

customers are not charged for both capitalized Allowance for Funds Used During Construction (AFUDC) and CWIP.<sup>9</sup>

**C. 150-Basis Point ROE Adder**

11. Duquesne requests a transmission rate incentive ROE adder of 150-basis points above Duquesne's currently effective ROE of 11.4 percent, which will result in an ROE of 12.9 percent for the Brady Project. Duquesne requests that this ROE adder be in effect until Duquesne joins the MISO. Duquesne states that when it withdraws from PJM, it will relinquish this ROE incentive and adopt the base ROE of 12.38 percent for all transmission assets authorized by the Commission for transmission owning members of MISO.

**D. Scope, Effect, Risks and Challenges**

12. Duquesne states that the Brady Project involves financial risk because of the magnitude of the capital commitment of \$291 million, which is approximately 95 percent of its December 31, 2007 net transmission plant in service of \$309.7 million. In addition, Duquesne notes that its Standard & Poor's rating is barely investment grade at BBB- with a negative outlook. Duquesne further states that it faces siting risks due to the construction of a major transmission expansion in an urban setting where the company has not yet obtained all of the necessary permits. In addition, Duquesne states that two major river crossings pose environmental and permitting risks. Finally, Duquesne notes that it faces the challenge of completing the Brady Project within PJM's RTEP tight timeframe.

**E. Total Package of Incentives**

13. Duquesne states that its request for an ROE adder of 150-basis points and its request for 100 percent recovery of CWIP are not mutually exclusive. Duquesne states that the recovery of CWIP in rate base is appropriate during the capital-intensive construction phase of the Brady Project. However, Duquesne notes that receiving the incentive for CWIP is unlikely to affect investor's perceptions of Duquesne's risks. Duquesne further states that the 150-basis point adder is justified given the combined impact of the DTEP and the Brady Project on its finances. Finally, Duquesne notes, unlike in its request for incentives in the DTEP proceeding, it not requesting the ability to recover any costs should abandonment occur.

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<sup>9</sup> Citing *Duquesne*, 118 FERC ¶ 61,087 at P 76. See also *American Electric Power Service Corp.*, 116 FERC ¶ 61,059 (2006); *American Transmission Co.*, 105 FERC ¶ 61,388, at P 39 (2003); *Boston Edison Co.*, 109 FERC ¶ 61,300 (2004).

## **F. Technology Statement**

14. Duquesne states that it is not specifically requesting incentives for the deployment of advanced transmission technologies. However, Duquesne states that it is deploying a number of innovative technology enhancements in the design of the Brady Project that it believes support the requested incentives.

15. Duquesne states that much of the Brady Project incorporates high-voltage 138-kV and 345-kV underground cables with forced cooling technology. Duquesne says the use of the underground cable will make the project siting possible and practical, facilitate acceptance of the project along the urban routes, and help avoid substantial, costly, and time consuming condemnations. New 3,000 MCM copper layered polypropylene paper cable conductors with skidwire will be used on 138-kV lines along with slow circulation technology and forced liquid cooling within the conduit to obtain a minimum continuous rating of 1,500 amperes on several circuits. In addition, four cooler stations will be installed. Duquesne states that use of these conductors will allow it to achieve higher contingent thermal line ratings with 40 percent more capacity than would be possible with a static system. Duquesne states that the final configuration will include five fluid pumping stations to maintain proper insulating fluid pressure and provide required fluid reserve capacity.

16. Duquesne adds that it will incorporate an Integrated Monitoring Diagnostic Alarm and Control System (MDACS) into the Brady substation that is designed for high-pressure fluid-filled cable systems. MDACS will provide monitoring, diagnostics, alarms, and real-time rating information that will provide remote access to plant operational status information to allow remote operation of the underground transmission systems.

17. Duquesne states that it will employ Gas Insulated Switchgear in a ring bus configuration for the Brady substation for all 345- and 138-kV line and transformer connections. This configuration reduces the land required for the substations by 75 percent compared to open-air alternatives and provides high reliability. Duquesne will also employ fiber optic technology in a SONET (Synchronous Optical NETWORK) ring configuration as opposed to a single path communications system. This ring configuration is used for high-speed line protection and SCADA (Supervisory Control and Data Acquisition) communications. It is more reliable than single path systems because if one path fails, the traffic is rerouted.

18. Duquesne states it will include state-of-the-art monitoring and diagnostic capability to provide instantaneous remote status information. This will include a microprocessor-based high-speed protective relays that have a self-diagnostic function that continuously monitors the relays' health and alerts Duquesne Operations staff through SCADA of any problem internal to the relay. At the Brady substation, there will also be hydrogen monitoring on the new 345/138-kV autotransformer to continuously

monitor its health. This monitor will be linked to the substation SCADA system so that Duquesne's maintenance staff can remotely track the autotransformer's condition.

19. Lastly, Duquesne states that the Brady Substation will have a battery charger capable of supplying the entire continuous DC load and blocking diodes to protect the substation DC supply by ensuring continuous DC power if there is a failure of either the battery or its charger. The combination protects against a single component failure of the DC system.

### **III. Procedural History, Notice of Filings and Responsive Pleadings**

20. Notice of Duquesne's filing was published in the *Federal Register*, 73 Fed. Reg. 50,607 (2008), with interventions and comments due on or before September 4, 2008.

21. Timely motions to intervene, raising no substantive issues, were filed by Exelon Corporation; Pepco Holdings, Inc.; Allegheny Power and Trans-Allegheny Interstate Line Company; Ameren Services Company; PJM; Great River Energy; Old Dominion Electric Cooperative; Duquesne Industrial Intervenors; PSEG Companies; and Consumers Energy Company. A motion to intervene and protest concerning the proposed 12.9 percent ROE was filed by the Pennsylvania Office of Consumer Advocate (Pennsylvania Consumer Advocate). On September 19, 2008, Duquesne filed an answer to the protest of the Pennsylvania Consumer Advocate.

### **IV. Discussion**

#### **A. Procedural Matters**

22. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2008), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

23. Rule 213(a) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2008), prohibits an answer to protests, unless otherwise ordered by the decisional authority. We are not persuaded to accept Duquesne's answer and therefore reject it.

#### **B. Section 219 Requirements**

24. In the Energy Policy Act of 2005 (EPAc 2005),<sup>10</sup> Congress added section 219 to the FPA, directing the Commission to establish, by rule, incentive-based rate treatments to promote capital investment in transmission infrastructure. The Commission subsequently issued Order No. 679, which sets forth processes by which a public utility

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<sup>10</sup> Pub. L. No. 109-58, 119 Stat. 594, § 1241.

could seek transmission rate incentives pursuant to section 219, including the incentives requested here by Duquesne.

25. Pursuant to section 219, an applicant must show that “the facilities for which it seeks incentives either ensure reliability or reduce the cost of delivered power by reducing transmission congestion.” Also, as part of this demonstration, “section 219(d) provides that all rates approved under the Rule are subject to the requirements of sections 205 and 206 of the FPA, which require that all rates, charges, terms and conditions be just and reasonable and not unduly discriminatory or preferential.”<sup>11</sup>

26. Order No. 679 provides that a public utility may file a petition for declaratory order or a section 205 filing to obtain incentive rate treatment for transmission infrastructure investment that satisfies the requirements of section 219, i.e., the applicant must demonstrate that the facilities for which it seeks incentives either ensure reliability or reduce the cost of delivered power by reducing transmission congestion.<sup>12</sup> Order No. 679 established a process for an applicant to follow to demonstrate that it meets this standard, including a rebuttable presumption that the standard is met if: (1) the transmission project 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) a project has received construction approval from an appropriate state commission or state siting authority.<sup>13</sup> Order No. 679-A clarifies 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.<sup>14</sup>

27. The Commission finds that the Brady Project satisfies the requirements for a rebuttable presumption for eligibility for transmission incentives under section 219. The Brady Project has been vetted and approved as part of PJM’s 2007 RTEP, which constitutes “a fair and open regional planning process.”<sup>15</sup> Moreover, the Commission finds that there is substantial evidence that these projects ensure reliability. Specifically, the Brady substation and associated transmission upgrades will improve reliability by

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<sup>11</sup> Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 8 (citing 16 U.S.C. §§ 824(d) and 824(e)).

<sup>12</sup> 18 C.F.R. § 35.35(i) (2008).

<sup>13</sup> Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 58.

<sup>14</sup> *Id.* P 49.

<sup>15</sup> *Virginia Electric and Power Co.*, 124 FERC ¶ 61,207, at P 32 (2008) (*VEPCO*).

completing a 345-kV ring around Pittsburgh. In addition, the Brady Project will provide transmission load relief, replace aging equipment, and provide new switching capabilities for critical load in Pittsburgh and Oakland. Finally, the new 3,000 MCM copper layered polypropylene paper cable (with a continuous rating of 1,500 amperes summer normal) will provide 40 percent more capacity compared to the current cable ratings (1,050 amperes summer normal).<sup>16</sup>

28. In addition, as Duquesne notes, the construction of the Brady Project will allow Duquesne to: (1) relieve identified N-1<sup>17</sup> overloads on Duquesne's underground, forced-cooled 345-kV cables beginning in the 2012 study period; (2) relieve N-2 overloads on Duquesne's underground 138-kV cables; (3) relieve N-1 overloads on Duquesne's underground forced-cooled 345-kV cables beginning in the 2022 study period; (4) replace its aging components at the Forbes 68-kV Substation, which is expected to reach "end of life" by 2015, with a new 138-kV Gas Insulated Switchgear; and (5) replace old 69-kv underground transmission cable with higher rated 138-kV and 345-kV cable.<sup>18</sup>

### C. The Nexus Requirement

29. 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."<sup>19</sup> The Commission noted that this nexus test is fact-specific and requires the Commission to review each application on a case-by-case basis.

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<sup>16</sup> Duquesne's filing, Exhibit No. DCL-1 at 6-8.

<sup>17</sup> Bulk power system must be capable of supplying power reliably under various conditions of demand and transmission system configurations. The N-1 criterion refers to the ability of the bulk power system to withstand loss of the most severe single element (e.g., a generator, a transmission line, or a transformer) without causing overload, low voltages, or system instability on the power system, or loss of customer load. The N-2 criterion is a higher level of power system security, where the system can withstand failure of any two elements (e.g., a generator and a transmission line or two transmission lines together) without causing overload, low voltages, or system instability on the power system, or loss of customer load.

<sup>18</sup> Duquesne's filing, Exhibit No. DLC-1 at 6.

<sup>19</sup> Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 40.

30. As part of this evaluation, the Commission has found the question of whether a project is routine to be particularly probative.<sup>20</sup> In *BG&E*, the Commission elaborated on how it will evaluate projects to determine whether they are routine and the effect this evaluation has on an applicant's request for incentives:

[W]e held in Order No. 679 that routine investments “may not always qualify” for incentives. However, the Commission did not find that they would never qualify. Similarly, in Order No. 679-A, we held that projects with “special risks and challenges” present “the most compelling case” for incentives, but did not hold they are the only projects that can qualify for incentives. Second, we held that routine investments “to meet existing reliability standards” may not always qualify for incentives. However, we did not hold that, if a project's primary or sole purpose is to maintain reliability, it should not be eligible for incentives. Indeed, to do so would have been to disregard the plain language of section 219, which required the Commission to adopt a rule that “promote[s] reliable and economically efficient transmission and generation of electricity by promoting capital investment in the enlargement, improvement, maintenance, and operation of all facilities for the transmission of electric energy in interstate commerce.”<sup>21</sup>

31. The Commission further stated that it will consider all relevant factors presented by an applicant to determine whether a project is routine; and the applicant must provide detailed factual information in support of the factors it relied upon. The relevant factors to be considered as part of the analysis of whether a project is routine include, but are not limited to: (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).<sup>22</sup> Additionally, the Commission clarified 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.”<sup>23</sup> Finally, the Commission stated that if it determines that a project is routine, an applicant is not foreclosed from the requested

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<sup>20</sup> *Baltimore Gas and Electric Co.*, 120 FERC ¶ 61,084, at P 48 (2007) (*BG&E*).

<sup>21</sup> *Id.* P 51 (footnotes omitted).

<sup>22</sup> *Id.* P 52-55.

<sup>23</sup> *Id.* P 54.

incentive; it may show that its project faces risks and challenges or provides sufficient benefits to warrant incentive rate treatment.<sup>24</sup>

32. As discussed below, the Commission finds that the Brady Project satisfies the nexus requirement. Duquesne is undertaking considerable risks and challenges to develop and construct its projects. It has demonstrated a nexus between those risks and challenges and the incentives that it has requested for the project.

#### **D. Incentive for CWIP**

33. Duquesne requests 100 percent recovery of CWIP costs for the Brady Project. Duquesne notes that recovery of CWIP will be through its formula transmission rate. Duquesne contends that allowing 100 percent recovery of CWIP will enhance its cash flow and help ensure timely completion of the Brady Project. Duquesne notes that its bond ratings are just above investment grade and that Standard & Poor's recently reduced its outlook to "negative." Duquesne states that another lowering of its bond ratings would increase its cost of borrowing and reduce its access to financial markets.<sup>25</sup>

34. Duquesne further states that allowing 100 percent recovery of CWIP will lessen the rate impact on its transmission customers as compared to AFUDC treatment.<sup>26</sup> Duquesne states that it will abide by the detailed accounting protocols to track expenditures on incentive projects to ensure that there is no double recovery of AFUDC through CWIP.<sup>27</sup> Duquesne proposes to continue those accounting protocols and to submit annual information reports to the Commission and its customers, if requested, for review.

35. In Order No. 679, the Commission established a policy that allows utilities to include, where appropriate, 100 percent of prudently-incurred transmission-related CWIP

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<sup>24</sup> *Id.* P 55.

<sup>25</sup> Duquesne filing, Exhibit No. DLC-1 at 26.

<sup>26</sup> *Construction Work in Progress for Public Utilities; Inclusion of Costs in Rate Base*, Order No. 298, FERC Stats. & Regs. ¶ 30,455 (1983), *order on reh'g*, Order No. 298-B, FERC Stats. & Regs. ¶ 30,524 (1983).

<sup>27</sup> Duquesne filing at 26. These protocols require Duquesne, in a future FPA section 205 filing, to implement a stand-alone balancing account mechanism to recover the CWIP revenue requirements and provide a detailed explanation of its accounting methods and procedures to: (1) implement the stand-alone balancing account; (2) comply with 18 C.F.R. § 35.13(h)(38) and § 35.25; and (3) maintain comparability of financial information.

costs in their rate base.<sup>28</sup> It noted that this rate treatment will further the goals of section 219 by providing up-front regulatory certainty, rate stability, and improved cash flow for applicants thereby reducing the pressures on their finances caused by investing in transmission projects.<sup>29</sup> We find that Duquesne has shown a nexus between the proposed CWIP incentive and its investment in the Brady Project. Duquesne's costs for the Brady Project of \$291 million will almost double its net transmission plant.

36. Consistent with Order No. 679, we find that authorizing 100 percent recovery of CWIP for the Brady Project will enhance Duquesne's cash flow, which will reduce the risk of a downgrade in debt ratings. Considering the relative size of Duquesne's \$291 million investment in the Brady Project, on top of its \$220 million investment in the DTEP, we find that authorization of the CWIP incentive for the Brady Project is appropriate.

37. We also find that allowing Duquesne to recover 100 percent of CWIP in its rate base will result in better rate stability for customers. As we have explained in prior orders,<sup>30</sup> 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 CWIP in rate base, the rate impact of the Brady Project can be spread over the entire construction period and will help consumers avoid a return on and of capitalized AFUDC.<sup>31</sup>

#### **E. 150-Basis Point ROE Adder**

38. Duquesne seeks authorization of a 150-basis point ROE adder due to significant risks and challenges faced by the Brady Project. We find that Duquesne has shown a nexus between the 150-basis point ROE adder requested for the Brady Project and the scope, risks and challenges faced by Duquesne in constructing the Brady Project.

39. In addition, we find that the Brady Project poses demonstrable risks and challenges. The scope of the Brady Project is significant due to the magnitude of Duquesne's capital commitment of \$291 million, which is approximately 95 percent of its December 31, 2007 net transmission plant in service of \$309.7 million. Indeed, its average annual capital expenditures on transmission will increase 16-fold, from about

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<sup>28</sup> Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 29, 117.

<sup>29</sup> *Id.* P 115.

<sup>30</sup> *See, e.g., American Electric Power Service Corp.*, 116 FERC ¶ 61,059, at P 59 (2006) (*AEP*), *order on reh'g*, 118 FERC ¶ 61,041, at P 27 (2007).

<sup>31</sup> *AEP*, 116 FERC ¶ 61,059 at P 59.

\$6 million a year over the past five years to about \$95 million per year over the next five years, due to the combined costs of the DTEP and the Brady Project.<sup>32</sup>

40. Furthermore, we find that the effect of the Brady Project will be to improve reliability by: (1) adding a second independent transmission route into Pittsburgh; (2) completing a 345-kV ring around Pittsburgh; (3) relieving load on existing 345-kV underground cables; and (4) allowing Duquesne to better accommodate west-to-east regional power flows across its system. This increased reliability will support the needs of Pittsburgh's hospitals, universities, manufacturing facilities and corporate headquarters.

41. Duquesne also faces regulatory and siting risks and challenges in completing the Brady Project. For example, the Brady Project includes the construction of a major transmission expansion with a substantial underground component in an urban setting. In addition, Duquesne has not yet obtained all of the necessary permits or rights-of-way. Further, it faces environmental risks because the Brady Project will be constructed in densely populated areas and cross two major rivers.

42. We further find that Duquesne faces economic risks because it must complete the Brady Project in an economic environment in which the costs of basic materials and labor are rising. For example, based on recent trends, Duquesne states that there has been a substantial rise in the cost of copper-related materials.<sup>33</sup> Further, Duquesne states that there is uncertainty regarding the acquisition and approval of the heavy-duty commercial building that will house the new Brady substation.

43. We find that Duquesne faces financial risks. It will finance the capital investments for the Brady Project with a combination of cash from operations, borrowed funds (i.e., bank borrowings and the issuance of long-term debt securities), and equity infusions from its owners. The equity investment must be part of the overall financing package for both the DTEP and the Brady Project because the projects are too large to fund through debt financing alone. In order to cover debt service, Duquesne states that it will need to raise external capital by issuing tax-exempt Pollution Control Revenue Bonds and taxable First Mortgage Bonds.<sup>34</sup>

44. Additional financial risks are due to Duquesne's ratings. Standard & Poor's "Issuer" rating for Duquesne is BBB- with a negative outlook and its Moody's "long-term" rating is Baa2 with a stable outlook. The Standard & Poor's rating places

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<sup>32</sup> Duquesne's filing, Exhibit No. DLC-1 at 5.

<sup>33</sup> Duquesne's filing, Exhibit No. DLC-1 at 13.

<sup>34</sup> Duquesne's filing, Exhibit No. DLC-8 at 6-9.

Duquesne in the bottom quartile of its peer group of regulated electric utilities. A lowering of Duquesne's Standard & Poor's rating would cause it to be below investment grade. Specifically, a one-notch downgrade in a credit rating could cost it approximately 50-basis points under its current unsecured revolving credit agreement,<sup>35</sup> and a credit rating downgrade can limit its ability to raise funds in capital markets.<sup>36</sup>

45. We find that the additional transmission revenues produced through the requested incentives would generate additional cash flow to support Duquesne's coverage ratios and its ability to service its debt. This, in turn, would help preserve Duquesne's credit quality and avoid an increase in rates for credit. We agree with Duquesne that absent the requested incentives, the additional debt assumed to fund the Brady Project would put downward pressure on the credit metrics for interest coverage (i.e., fund from operations divided by interest expense) and leverage (i.e., funds from operations divided by debt) which could then negatively impact Duquesne's credit ratings. This would increase Duquesne's future borrowing costs and, ultimately, lead to higher rates for its customers.<sup>37</sup>

#### **F. Total Package of Incentives**

46. As noted above, in Order No. 679-A, the Commission clarified that its 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. The Commission noted that this nexus test is fact-specific and requires the Commission to review each application on a case-by-case basis. Consistent with Order No. 679,<sup>38</sup> the Commission has, in prior cases, approved multiple rate incentives for particular projects.<sup>39</sup> This is consistent with our interpretation of FPA section 219 as authorizing the Commission to approve more than one incentive rate treatment for an applicant proposing a new transmission project, as long as each incentive is justified by a showing that it satisfies the requirements of the FPA section 219 and that there is a nexus between the incentives being proposed and the investment being made.

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<sup>35</sup> Duquesne's filing, Exhibit No. DLC-8 at 11.

<sup>36</sup> *Id.*

<sup>37</sup> *Id.* at 11-12.

<sup>38</sup> Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 55.

<sup>39</sup> *See, 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).

47. Duquesne states that its request for an ROE adder of 150-basis points and its request for 100 percent recovery of CWIP are not mutually exclusive. It notes that CWIP changes the timing – not the level – of cost recovery.<sup>40</sup> With a required June 2012 in-service date, Duquesne states that the recovery of CWIP in rate base is appropriate during the capital-intensive construction phase of the Brady Project. Further, CWIP recovery reduces the rate impact on customers when the Brady Project is placed into service. However, Duquesne states that receiving the incentive for CWIP is unlikely to affect investor's perceptions of Duquesne's risks. Duquesne submits that the two incentives are not mutually exclusive and strike an appropriate balance given the overall risks and challenges of the Brady Project. Duquesne states that the 150-basis point adder is justified given the combined impact of the DTEP and the Brady Project on its finances. Duquesne's currently lower credit rating, PJM's aggressive timetable for completing the Brady Project, and the fact that Duquesne is not requesting the ability to recover any costs should abandonment occur.

48. The Commission further finds that Duquesne has demonstrated the interrelationship between its requested incentives for the Brady Project and the impact of those incentives on its cash flow and credit ratings. Duquesne stated that this interrelationship between the Brady Project and the DTEP impacts its credit and ability to finance both projects. Indeed, Duquesne's costs for the Brady Project of \$291 million and \$220 million for the DTEP, represent approximately 94 percent and 71 percent, respectively, of its net transmission plant of \$309.7 million as of December 31, 2007. These two projects, which are among the largest projects ever undertaken by Duquesne, will increase its net transmission plant in service by 165 percent. The Brady Project and the DTEP are separate but complimentary projects which complete a high-voltage ring around Pittsburgh and enhance reliability in the Duquesne's service territory. The incentives requested here are tailored to the Brady Project, while the incentives requested in the DTEP proceeding were tailored to that project. Although for the DTEP, Duquesne asked for an ROE adder of 150-basis points, 100 percent recovery of CWIP, 100 percent recovery of prudently-incurred pre-construction costs, and the recovery of prudently-incurred costs due to abandonment for reasons beyond its managements control, the Commission reduced the ROE adder to 100-basis points and granted the other three project-specific incentives (plus 50-basis points for PJM membership). In this proceeding, Duquesne did not request the pre-construction and abandonment incentives, but instead requested an additional 50-basis points for the ROE adder in recognition of the increased financial risks due to the two projects.

49. In sum, we find that Duquesne has shown that the total package of incentives is tailored to address the demonstrable risks or challenges faced by Duquesne.<sup>41</sup> The

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<sup>40</sup> Duquesne's filing, Exhibit No. DLC-9 at 6-7.

<sup>41</sup> Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 21, 27.

incentive rate treatments proposed by Duquesne are not mutually exclusive. Further, Duquesne has explained why it is seeking each incentive and how each is relevant to the proposed Brady Project. As discussed above, we find that Duquesne faces demonstrable risks and challenges in constructing the Brady Project. We find here that granting the 150-basis point ROE incentive and 100 percent recovery of CWIP will encourage investors to invest in a transmission project with substantial financial risks, like the Brady Project.

## **G. ROE for the Brady Project**

### **1. Duquesne's Proposal**

50. Duquesne contends that with its requested ROE adder of 150-basis points, the resulting ROE of 12.9 percent for the Brady Project is within the zone of reasonableness for the cost of its equity. In support, Duquesne states that it applied a discounted cash flow analysis (DCF) consistent with the methodology prescribed in *PATH*<sup>42</sup> and the guidance provided by the Commission in *Southern California Edison Co.* and *Consumers Energy Co.*<sup>43</sup> Duquesne states that its DCF included: (1) companies that are transmission owning companies operating in the northeast region of the United States; (2) companies that have a Standard & Poor's (or Moody's) credit quality rating equivalent to, one notch above, or one notch below the ratings for Duquesne; and (3) companies that have earnings growth rates that are sustainable.<sup>44</sup>

51. Then, consistent with *PATH*, Duquesne eliminated those utilities whose Standard & Poor's or Moody's credit ratings were not either one rating above or below its rating of BBB- (Standard & Poor's) and Baa2 (Moody's). That resulted in a proxy group of utilities with an Standard & Poor's corporate credit rating between BB+ to BBB (or Moody's equivalent), which consists of American Electric Power, Dominion Resources,

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<sup>42</sup> *Potomac-Appalachian Transmission Highline, L.L.C.*, 122 FERC ¶ 61,122, at P 95-105 (2008) (*PATH*).

<sup>43</sup> *Southern California Edison Co.*, 122 FERC ¶ 61,187 (2008); *Consumers Energy Co.*, 98 FERC ¶ 61,333 (2002).

<sup>44</sup> Consistent with the methodology prescribed in *PATH*, Duquesne used a starting sample of publicly-owned companies in PJM, NYISO and ISO-NE. However, Duquesne's sample includes the utilities identified in *PATH* (American Electric Power Co., Central Vermont Public Service, Consolidated Edison, Inc., Constellation Energy Group, Dominion Resources, DPL Inc., Exelon Corp., FirstEnergy Corp., FPL Group, Inc., Northeast Utilities, NSTAR, Pepco Holdings, Inc., PPL Corporation, Public Service Enterprise Group, and UIL Holdings) plus Allegheny Energy Inc. and CH Energy Group, Inc.

DPL Inc., Exelon Corp., FirstEnergy Corp., Northeast Utilities and Public Service Enterprise Group Inc. Based on this proxy group, Duquesne states that the zone of reasonable returns for its cost of equity is 9.46 percent to 16.38 percent.

52. Duquesne does not propose to change its base ROE of 11.4 percent, which was accepted by the Commission in the Order Accepting Uncontested Settlement.

## 2. Protests

53. The Pennsylvania Consumer Advocate notes that under the uncontested settlement, Duquesne receives a base ROE of 11.4 percent for all projects, except for the DTEP, for which it receives an ROE of 12.4 percent. The Pennsylvania Consumer Advocate contends that Duquesne has not satisfactorily explained why a higher ROE is necessary for the Brady Project compared to the DTEP. The Pennsylvania Consumer Advocate states that the 12.9 percent ROE for the Brady Project seems arbitrary. It further notes that Duquesne does not acknowledge the risk-reducing effect of having formula transmission rates. However, it contends that without further justification, an ROE of 12.9 percent may lead to rates that are unjust and unreasonable.

## 3. Commission Determination

54. No party objected to Duquesne's proposed zone of reasonableness. The Pennsylvania Consumer Advocate, however, protested the level of Duquesne's ROE.

55. The Commission finds that Duquesne did not fully conform to the guidelines set forth in *PATH*. For example, the appropriate credit rating screening criteria require that each utility included in the proxy group have a Standard & Poor's corporate credit rating from BB+ to BBB (or the equivalent Moody's rating).<sup>45</sup> Accordingly, Dominion Resources and Exelon Corp. should be excluded from the proxy group because their credit ratings are higher than BBB, and PPL Group should be included because its credit rating is BBB. Further, Duquesne failed to accurately compute the adjustment factor for growth rates. Duquesne's adjustment factor was calculated using the forward projected 2009 and 2012 numbers. Duquesne should have computed the adjustment factor using actual 2007 data and projected 2011-2013 data. These adjustments result in a change to the zone of reasonableness; the adjusted zone is 8.51 percent to 15.62 percent.

56. Using the data prepared by Duquesne and revising the proxy group to reflect the *PATH* methodology, the Commission finds that an ROE of 12.9 percent for the Brady Project falls within the zone of reasonableness.

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<sup>45</sup> *PATH*, 122 FERC ¶ 61,188 at P 98.

57. We are not persuaded by the Pennsylvania Consumer Advocate's protest. As explained *supra*, we considered the risks presented by the Brady Project by itself and in conjunction with the DTEP. Based on the evidence in the record, we find that the risks, especially the financial risks of completing two major projects which will more than double Duquesne's net transmission plant in service, warrant an ROE adder of 150-basis points for the Brady Project. We have also considered the requested incentives for the Brady Project together with Duquesne's formula rate. We find that the requested incentives and the formula rate are not mutually exclusive but together will encourage investors to invest in a variety of transmission projects.<sup>46</sup>

#### H. Technology Statement

58. Duquesne has satisfied Order No. 679's technology statement requirement in providing a description of the advanced technologies that were considered, and an explanation as to why these particular technologies were chosen over other alternatives.

#### The Commission orders:

(A) Duquesne's revised tariff sheets are hereby accepted for filing, to become effective on October 13, 2008, as requested, as discussed in the body of this order.

(B) Duquesne's September 19, 2008 answer is hereby rejected.

By the Commission. Commissioner Kelly dissenting with a separate statement attached.  
Wellinghoff dissenting in part with a separate statement attached.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.

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<sup>46</sup> *VEPCO*, 124 FERC ¶ 61,207 at P 113 (2008) (*VEPCO*).

UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Duquesne Light Company

Docket No. ER08-1402-000

(Issued October 10, 2008)

KELLY, Commissioner, *dissenting*:

This order addresses a request for incentive rate treatment filed by Duquesne Light Company (Duquesne). Duquesne requests two transmission rate incentives for the Brady Project: a return on equity (ROE) incentive adder of 150-basis points and recovery of 100 percent of its costs for construction work in progress (CWIP). I dissent from this order.

I applied the project-based criteria that I have relied upon in previous transmission incentives proceedings in order to determine whether the Brady project warrants incentive rate treatment.<sup>1</sup> Based on those criteria, I conclude that it does not. As I determined in a previous Duquesne incentives application,<sup>2</sup> the Brady Project appears to fall into the category of “routine investments made in the ordinary course” that was discussed in Order No. 679-A.<sup>3</sup>

First, I do not believe that the Brady Project offers broad regional benefits to the public interest. My review of the application indicates that Duquesne proposes to undertake routine investments in transmission facilities in order to maintain reliable service. Duquesne asserts that the Brady Project “and related 345 kV and 138 kV system upgrades that are essential to maintaining reliable service to the City of Pittsburgh, Pennsylvania, and surrounding region.”<sup>4</sup> While this is a useful project, it does not bring broad-ranging benefits to the public

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<sup>1</sup> See *American Electric Power Service Corporation*, 118 FERC ¶ 61,041 (2007).

<sup>2</sup> *Duquesne Light Co.*, 118 FERC ¶ 61,087 (2007).

<sup>3</sup> Order No. 679-A, 117FERC ¶ 61,345 at P 60.

<sup>4</sup> Exhibit No. DLC-1 at p 2.

interest deserving of incentive rate treatment. Second, the geographic scope of the project and the fact that Duquesne has existing rights-of-way for much of the project<sup>5</sup> means that Duquesne's regulatory authorizations will be limited in scope and limited to obtaining local approvals. Third, while the size of the investment may be proportionally large for a company like Duquesne, it nevertheless appears routine in that Duquesne must complete this project in order to continue to reliably serve its own customers in the near future.

This is a project that is being undertaken in the ordinary course of Duquesne's business. Upgrading the transmission service in and around Pittsburgh to satisfy reliability criteria is part of Duquesne's core business, not something special or unique or subject to excessive risks or challenges. For such an investment, normal rate recovery, including the normal risk-based regulated return, should be wholly adequate.

Finally, I am somewhat mystified to find that the requested ROE adder will only apply while Duquesne is a member of PJM: "In the event that the Commission approves the integration of Duquesne into the Midwest ISO on acceptable terms and conditions in order to be able to consummate the integration, then Duquesne would propose not to recover any incremental ROE adder while a member of Midwest ISO."<sup>6</sup> Assuming for the sake of argument that Duquesne actually requires an incentive ROE adder to undertake the Brady Project, the ROE incentive is apparently, but inexplicably, only needed for as long as Duquesne remains a member of PJM. Duquesne effectively ties the incentive ROE adder to membership in a particular RTO rather than to the project identified in the application. Order No. 679 did not contemplate approving such requests, which looks more like than ROE shopping than anything else.

Accordingly, I respectfully dissent in part from this order.

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Suedeen G. Kelly

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<sup>5</sup> Exhibit No. DLC-1 at p 11.

<sup>6</sup> Exhibit No. DLC-1 at p 3.

UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Duquesne Light Company

Docket No. ER08-1402-000

(Issued October 10, 2008)

WELLINGHOFF, Commissioner, dissenting in part:

As I have stated before, I believe that the majority's approach to reviewing requests for incentive ROE adders severely undermines the nexus requirement that is an essential component of Order No. 679. I also continue to believe that the majority places inadequate emphasis on the proposed use of advanced technologies in assessing the risks and challenges that may warrant an incentive ROE adder for a project.<sup>1</sup> Because today's order further illustrates both problems, I respectfully dissent in part.

With respect to the first of these problems, the majority finds that Duquesne has shown a nexus between the 150 basis point incentive ROE adder requested for the Brady Project and the scope, risks, and challenges that Duquesne faces in constructing the project.<sup>2</sup> Unfortunately, several of the majority's statements in support of that finding could be made about virtually any project. For example, the majority states that the increased reliability resulting from the Brady Project will support the needs of "hospitals, universities, manufacturing facilities, and corporate headquarters."<sup>3</sup> Without diminishing the importance of those benefits, it is difficult to see how the majority's statement serves to distinguish projects that warrant an incentive ROE adder from those that do not.

Similarly, the majority finds that "Duquesne faces economic risks because it must complete the Brady Project in an economic environment in which the costs of basic materials and labor are rising."<sup>4</sup> Any utility could make that statement about literally any project that it is pursuing at present. The majority's willingness to grant an incentive ROE adder based on a statement that, while factually accurate, would apply to any application before the Commission starkly illustrates how inappropriately low the majority has set the bar for the nexus requirement of Order No. 679.

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<sup>1</sup> See, e.g., *Commonwealth Edison Co.*, 122 FERC ¶ 61,037 (2008) (dissent in part of Commissioner Wellinghoff); *Virginia Elec. and Power Co.*, 124 FERC ¶ 61,207 (2008) (dissent of Commissioner Wellinghoff).

<sup>2</sup> *Duquesne Light Co.*, 125 FERC ¶ 61,028 at P 38 (2008).

<sup>3</sup> *Id.* P 40.

<sup>4</sup> *Id.* P 42.

With respect to the second problem noted above, I am disappointed that the majority's consideration of the technology statement that Duquesne submitted in accordance with Order No. 679 is limited to a single sentence at the end of today's order. The majority states that "Duquesne has satisfied Order No. 679's technology statement requirement in providing a description of the advanced technologies that were considered, and an explanation as to why these particular technologies were chosen over other alternatives."<sup>5</sup> This approach places inadequate emphasis on the proposed use of advanced technologies in determining whether a project warrants an incentive ROE adder. It also stands in sharp contrast to the analysis that the Commission recently conducted with respect to another request for an incentive ROE adder.<sup>6</sup>

As I have discussed previously, I believe that consideration of advanced technologies and their associated risks and challenges is an appropriate component of the nexus analysis that the Commission conducts in evaluating applications for incentives under Order No. 679.<sup>7</sup> Based on my review of Duquesne's application, including the above-noted technology statement, I would grant Duquesne a 50 basis point incentive ROE adder to account for risks and challenges associated with the Brady Project. This level of incentive is consistent with my previous statements regarding projects using underground cable technology on a 345 kV transmission line.<sup>8</sup>

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<sup>5</sup> *Id.* P 58.

<sup>6</sup> *New York Regional Interconnect, Inc.*, 124 FERC ¶ 61,259 at P 42-57 (2008).

<sup>7</sup> *See, e.g., Potomac-Appalachian Transmission Highline, L.L.C.*, 122 FERC ¶ 61,188 (2008) (dissent in part of Commissioner Wellinghoff at 1-4); *Northeast Utilities Service Co.*, 124 FERC ¶ 61,044 (2008) (dissent of Commissioner Wellinghoff at 2-3).

<sup>8</sup> *See The United Illuminating Co.* 119 FERC ¶ 61,182 (2007) (dissent in part of Commissioner Wellinghoff); *Northeast Utilities Service Co.*, 124 FERC ¶ 61,044 (2008) (dissent of Commissioner Wellinghoff). I note that this level of incentive is less than I supported for a previous Duquesne project. *See Duquesne Light Co.*, 118 FERC ¶ 61,087 (2007). In my concurrence in part and dissent in part to that order, I agreed with the Commission's decision to grant Duquesne a 100 basis point adjustment for part of the subject project. I also stated that I expected to see a more thorough evaluation of the feasibility of using state-of-the-art technologies in any future petition for declaratory order seeking incentive rate treatments. Although the technology statement in Duquesne's filing underlying today's order provides greater detail than appeared in some other recent applications to the Commission, it does not meet the standard that I described in my previous statement. I continue to encourage future applicants for incentive ROE adders to provide more detailed information on this important issue.

For these reasons, I respectfully dissent in part.

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Jon Wellinghoff  
Commissioner