

133 FERC ¶ 61,034  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Marc Spitzer, Philip D. Moeller,  
John R. Norris, and Cheryl A. LaFleur.

Pinnacle West Capital Corp.

Docket No. TX02-1-003

ORDER DENYING REHEARING

(Issued October 12, 2010)

1. In this order, we deny requests for rehearing and clarification of an order issued on May 17, 2010 that accepted, subject to modification, a proposal by Electrical District No. 3 of Pinal County, Arizona (ED3) to change the rate it charges the Arizona Public Service Company (APS) for transmission service from a stated rate to a formula rate.<sup>1</sup>

**I. Background**

2. ED3 provides transmission service to APS pursuant to Commission orders<sup>2</sup> under section 211 of the Federal Power Act (FPA).<sup>3</sup> In the 2002 Final Order, the Commission noted that ED3 and APS were able to reach agreement on the rates, terms, and conditions for providing service, and accepted a transmission service agreement between ED3 and APS which specified that ED3 would provide transmission service to APS at a stated rate of 15 mills per kWh.<sup>4</sup>

3. On July 15, 2008, ED3 filed an application with the Commission asserting that the stated rate of 15 mills per kWh no longer recovers ED3's cost of service and requesting a change from the stated rate to a formula rate. ED3 proposed to incorporate both its

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<sup>1</sup> *Pinnacle West Capital Corp.*, 131 FERC ¶ 61,143 (2010) (May 17, 2010 Order).

<sup>2</sup> *Pinnacle West Capital Corp.*, 98 FERC ¶ 61,039 (2002 Proposed Order), *final order*, 100 FERC ¶ 61,146 (2002) (2002 Final Order).

<sup>3</sup> 16 U.S.C. § 824j (2006).

<sup>4</sup> 2002 Final Order, 100 FERC ¶ 61,146 at P 9-10.

transmission and distribution facilities into the system average formula rate. ED3 also proposed to include: (1) a cost of capital developed utilizing ED3's actual cost of debt for each historical period, grossed-up by a margin requirement of 25 basis points; and (2) 100 percent of construction work in progress (CWIP) into the development of rate base.<sup>5</sup> ED3 requested an effective date of July 16, 2008 and voluntarily committed to refund, with interest, any amounts collected from APS that the Commission determined to exceed a just and reasonable rate.<sup>6</sup>

4. On March 2, 2009, the Director, Division of Tariffs and Market Development-West, acting pursuant to delegated authority, issued a letter to ED3 requesting additional information for the purpose of evaluating ED3's proposed rate change. On March 27, 2009, ED3 filed supplemental information. However, the information filed was not sufficient to enable the Commission to determine whether all of the facilities included in ED3's proposed system average formula rate were part of an integrated network system appropriate for rolled-in pricing. In an effort to expediently acquire the necessary data, the Commission issued a Technical Conference Notice on October 29, 2009 that requested ED3 to address a number of issues that would enable the Commission to determine whether rolled-in pricing is appropriate for all of the ED3 transmission and distribution facilities. Specifically, the Commission stated that "[s]upport for the issues identified above [in the Notice] should include color-coded system-wide and voltage level specific one-line diagrams, power flow and other completed system studies, long-term transmission plans, load forecast studies and any additional information that will assist Commission staff."<sup>7</sup>

5. On November 9, 2009, ED3 submitted additional materials. On November 19, 2009, Commission Staff held a technical conference for the limited purpose of obtaining additional information about the degree of integration of ED3's transmission and distribution system. Both ED3 and APS submitted post-technical conference initial and reply comments.

6. In the May 17, 2010 Order, the Commission accepted, subject to modification, ED3's proposed formula rate, finding that "the proposed ED3 formula rate, as modified by this order, strikes an equitable balance between ED3's need to recover the costs of providing transmission service to APS, on one hand, and APS's actual use of the ED3 system, on the other."<sup>8</sup> With regard to the proposed system average formula rate, the

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<sup>5</sup> ED3 Filing at 3-8.

<sup>6</sup> *Id.* at 10.

<sup>7</sup> Technical Conference Notice at 2.

<sup>8</sup> May 17, 2010 Order, 131 FERC ¶ 61,143 at P 1.

Commission approved rolled-in treatment for ED3's 69 kV (and higher voltage) facilities, but found that ED3 had not met its burden to demonstrate that its 12 kV (and lower voltage) distribution facilities were appropriate for roll-in.<sup>9</sup> Therefore, to enable ED3 to recover the costs of the lower voltage facilities, the Commission directed ED3 to "separately develop and submit a secondary distribution charge for jurisdictional distribution service, in which ED3 may recover costs associated with those eligible 12 kV (and lower voltage) facilities specified in Appendix A."<sup>10</sup> The Commission instructed ED3 to directly assign the costs of the eligible 12 kV facilities using facility-specific cost of service data.<sup>11</sup> The Commission denied ED3's request to include 100 percent of CWIP in rate base in its proposed formula rate, finding that ED3 had not made the showing required by Order No. 679,<sup>12</sup> which sets forth the requirements for recovery of 100 percent of CWIP.<sup>13</sup> The Commission did, however, permit recovery of 50 percent of CWIP in both the rolled-in pricing and the secondary distribution charge.<sup>14</sup> The Commission directed ED3 to incorporate the required modifications to its proposed formula rate in a compliance filing within 60 days of the May 17, 2010 Order.<sup>15</sup>

7. ED3 filed a timely request for rehearing and/or clarification. APS filed an answer.

## II. Request for Rehearing

8. ED3 argues that the Commission acted unreasonably and without substantial evidentiary support in finding that ED3 failed to meet its burden of demonstrating the justness and reasonableness of rolling in the costs of all of its 12 kV distribution facilities in its system average formula rate. ED3 asserts that the rationales offered by the Commission lack record support and are at odds with both the evidentiary record and Commission precedent. First, ED3 contends that it established at least two of the five

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<sup>9</sup> *Id.* P 41.

<sup>10</sup> *Id.* P 51.

<sup>11</sup> *Id.* P 50-51.

<sup>12</sup> *Promoting Transmission Investment through Pricing Reform*, Order No. 679, FERC Stats. & Regs. ¶ 31,222 (2006), *order on reh'g*, Order No. 679-A, FERC Stats. & Regs. ¶ 31,236, *order on reh'g*, 119 FERC ¶ 61,062 (2007).

<sup>13</sup> May 17, 2010 Order, 131 FERC ¶ 61,143 at P 56-58.

<sup>14</sup> *Id.* P 59-62.

<sup>15</sup> *Id.* P 51, 62. On July 1, 2010, pursuant to ED3's request, the Commission issued a notice of extension of time for ED3's compliance filing until October 17, 2010.

factors for integration set forth in *Mansfield Municipal Electric Dept., et al. v. New England Power Co.*, 97 FERC ¶ 61,134 (2001) (*Mansfield*).<sup>16</sup> Specifically, ED3 reiterates its prior assertion that it provides transmission service to itself over the facilities in question, thereby satisfying the third *Mansfield* factor. ED3 also asserts that it has demonstrated that both its 69 kV and 12 kV systems provide reliability benefits to its transmission system. ED3 argues that the Commission erred by “retreating from established Commission standards” without furnishing an explanation as to what standards were being used to supplant the *Mansfield* factors.<sup>17</sup>

9. ED3 further contends that the justifications for denying rolled-in treatment for the 12 kV (and lower voltage) facilities presented in the May 17, 2010 Order are “difficult to reconcile” with the Commission’s general position that “any degree of integration” is sufficient to permit recovery of facility costs through a rolled-in rate.<sup>18</sup> First, ED3 faults the Commission’s reliance on ED3’s ten-year transmission plan (Exhibit ED3-9) as evidence that the 12 kV system is not part of the integrated transmission system. According to ED3, the ten-year transmission plan is a function of state regulatory requirements and has no bearing on whether ED3 considers the 12 kV facilities to be part of its transmission system. ED3 asserts that the more relevant consideration is the fact that the Commission has required ED3 to provide “firm network transmission service over its electric transmission and distribution system of the same character and nature as the service that APS previously received from ED-3 under the lease agreement.”<sup>19</sup>

10. In addition, ED3 argues that the Commission offered no sound reasons for its finding that the 12 kV facilities do not provide a system-wide reliability benefit. ED3

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<sup>16</sup> Under the *Mansfield* framework, transmission facilities are considered to be integrated, thereby justifying rolled-in pricing, unless all five of the following factors are satisfied: (1) the facilities are radial, not looped; (2) energy flows in just one direction over the facilities at issue; (3) the applicant is able to serve only its own customers over these facilities; (4) the radial configuration prevents the applicant from providing support and added reliability to the other looped lines; and (5) an outage on any one of these facilities would not affect the power flows on the remainder of the system. Thus, a negative showing on even one of the factors is sufficient to demonstrate some degree of integration.

<sup>17</sup> ED3 Request for Rehearing in Docket No. TX02-1-003 at 7-8 (ED3 Rehearing Request).

<sup>18</sup> *Id.* at 9 (citing *Northeast Texas Elec. Coop.*, 108 FERC ¶ 61,084, at P 48 (2004) (*Northeast Texas*)).

<sup>19</sup> *Id.* at 10.

asserts that the Commission unreasonably enhanced ED3's burden of proof by requiring power flow studies to support ED3's claim that the 12 kV facilities provide system-wide reliability benefits. ED3 complains that the first express request for power flow studies appeared in the Technical Conference Notice, allowing only ten calendar days for ED3 to assemble a considerable quantity of information. Moreover, ED3 contends that the Commission has "regularly allowed rolled-in treatment of subtransmission facilities exhibiting the same characteristics as the Commission ascribes to ED3's distribution facilities."<sup>20</sup> ED3 maintains that, even without power flow studies, evidence in the record demonstrates conclusively that ED3's system is integrated because "each of the 12 kV circuits sought to be included in ED3's proposed formula rate provides 'backup' for the 12 kV system."<sup>21</sup> ED3 insists that the Commission's finding of no system-wide reliability benefit runs contrary to Commission precedent.<sup>22</sup>

11. Further, ED3 questions the Commission's focus on the "lopsided distribution" between APS customers and the bulk of the ED3 expansion in reaching its conclusion that rolling in the cost of the entire ED3 distribution system would be inequitable. ED3 asserts that there is no Commission precedent requiring uniform dispersal of customer loads to justify cost recovery through a rolled-in rate. Moreover, ED3 maintains that it demonstrated that its 12 kV facilities in the northeastern region of the ED3 footprint do serve APS customers, and emphasizes that the combined load of these customers is significant.<sup>23</sup>

12. In addition, ED3 argues that the Commission acted unreasonably and failed to engage in reasoned decision making in denying ED3's requested recovery of 100 percent of CWIP in rate base. ED3 asserts that the Commission erred by using the jurisdictional difference between the service provided by ED3 to its own retail customers and the

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<sup>20</sup> *Id.* at 11 (citing *Boston Edison Co.*, 61 FERC ¶ 61,026, at 61,131 n.1 (1992) (*Boston Edison*); *Allegheny Elec. Power Co.*, 122 FERC ¶ 61,160, at P 29-31 (2008) (*Allegheny*)).

<sup>21</sup> *Id.* at 12 (referring specifically to the contingency switching arrangements detailed in Exhibit ED3-44).

<sup>22</sup> *Id.* (citing *Northeast Texas Elec. Coop.*, 111 FERC ¶ 61,189, at P 42, n.66 (2005) ("The criterion we examine is simply whether other users receive a benefit, without regard to quantifying that benefit.") (*Northeast Texas Elec. Coop.*); *Sierra Pacific Power Corp. v. FERC*, 793 F.2d 1086, 1088 (9<sup>th</sup> Cir. 1986) (Integration exists "even where one of the parallel paths is normally operated 'opened,' that is, with the connection broken by opening a switch.") (*Sierra Pacific*)).

<sup>23</sup> *Id.* at 13-14.

service provided to APS pursuant to an FPA section 211 order as a basis for denying 100 percent CWIP recovery. ED3 argues that because the same facilities are used to provide service to both sets of customers, there is no justification for different treatment of CWIP in the respective rates charged for transmission. ED3 contends that using this distinction to justify denial of recovery of 100 of CWIP in rate base is both wrong and inattentive to the rationale underlying the 50 percent limitation in the context of investor-owned utilities. According to ED3, the reason for the limitation for investor-owned utilities is the conflict between the interests of the shareholders, who want to quickly realize a return on investment, and consumers who prefer to defer rate increases. ED3 maintains that, because it has no shareholders, and hence no conflict of interest, the 50 percent limitation cannot apply. ED3 appears to argue, therefore, that because it sees no conflict of interest, it is entitled to 100 percent CWIP recovery.<sup>24</sup>

13. Finally, ED3 asserts that the Commission erred by requiring ED3 to use facility-specific cost of service data in developing the secondary distribution charge. Thus, to the extent the Commission denies rehearing on the issue of rolled-in pricing for the 12 kV facilities, and to the extent the Commission intended to require ED3 to use facility-specific cost of service data to develop the secondary distribution charge, ED3 moves for clarification that it may, instead, use system average cost data in cases where facility-specific data prior to October 9, 2001 is in the possession of APS<sup>25</sup> and unavailable to ED3. In the alternative, ED3 requests rehearing on this issue.<sup>26</sup>

### **III. Discussion**

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

14. Rule 713(d)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d)(1) (2010), prohibits an answer to a request for rehearing. We will therefore reject APS' answer to ED3's request for rehearing.

#### **B. Rolled-In Treatment for 12 kV Facilities**

15. The Commission denies rehearing on the issue of whether ED3 may roll in the cost of its 12 kV facilities in the formula rate it charges APS. As a threshold matter, we note that even ED3 classifies the 12 kV facilities at issue as distribution facilities, not

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<sup>24</sup> *Id.* at 14-18.

<sup>25</sup> ED3 states that APS was ED3's transmission customer and the lessee of the ED3 system for the period from 1961 through October 9, 2001.

<sup>26</sup> ED3 Rehearing Request at 18-19.

transmission or subtransmission.<sup>27</sup> Subtransmission facilities are still transmission facilities, albeit toward the lower end of the voltage range for transmission facilities; they still perform the transmission function of delivering power on a localized basis to a distribution system<sup>28</sup> and are subject to the Commission's jurisdiction under sections 205 and 206 of the FPA.<sup>29</sup> Unlike the preference for rolled-in treatment of integrated network transmission or subtransmission facilities, distribution facilities are generally directly assigned, unless it can be shown that the distribution facilities are part of an integrated network.<sup>30</sup> Thus, we find that ED3's reliance on Commission precedent pertaining to rate structures for transmission or subtransmission facilities, including the *Mansfield* factors, is misplaced.

16. As we explained in the May 17, 2010 Order, we found that the *Mansfield* factors are not dispositive for resolving the question of whether ED3's 12 kV distribution facilities are part of an integrated transmission network. Indeed, *Mansfield* has traditionally been applied as a test for the integration of discrete transmission or subtransmission facilities, generally involving the integrity of the bulk power system.<sup>31</sup> Thus, the Commission did not arbitrarily depart from established precedent by declining to rely on *Mansfield* in this case. Rather, upon consideration of both the record in this case and the relevant precedent, the Commission concluded that the *Mansfield* framework is ill-suited to the resolution of this matter, and found that, "[g]iven the topology of the ED3 system and our understanding of its normal use, the *Mansfield* factors are inappropriate as a test for integration."<sup>32</sup> In its rehearing request, ED3 has failed to

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<sup>27</sup> See Ex. ED3-10 (color-coded system map) and Ex. ED3-6 at 4-5 (describing the 12 kV facilities as distribution lines)).

<sup>28</sup> *Boston Edison*, 61 FERC at 61,131 n.1; see also *Minnesota Power & Light Co.*, 21 FERC ¶ 61,233 (1982).

<sup>29</sup> See, e.g., *Allegheny*, 122 FERC ¶ 61,160.

<sup>30</sup> See, e.g., *Tex-La Elec. Coop. of Texas, Inc.*, 69 FERC ¶ 61,269, at 62,036 (1994) (*Tex-La*).

<sup>31</sup> See, e.g., *Northeast Texas*, 108 FERC ¶ 61,084 at P 50; *Alabama Power Co.*, 8 FERC ¶ 61,083, at 61,329 (1979); *Florida Power & Light Co.*, 99 FERC ¶ 61,197, at P 12 n.9 (2002) (all defining a transmission network as a system that moves energy in bulk); see also *Central Maine Power Co.*, 129 FERC ¶ 61,032, at P 1, 13 (2009); *Southern California Edison Co.*, 117 FERC ¶ 61,103, at P 72-73 (2006) (stating that *Mansfield* is the appropriate test for assessing whether 115 kV lines were network upgrades).

<sup>32</sup> May 17, 2010 Order, 131 FERC ¶ 61,143 at P 45.

demonstrate that the *Mansfield* factors should be applied as a test in deciding whether 12 kV distribution facilities are part of an integrated transmission network. Accordingly, we are not persuaded to reverse our determination and we reject ED3's continued insistence that its 12 kV system satisfies two of the *Mansfield* factors.

17. We also reject ED3's contention that the Commission failed to articulate or explain the standards used to reach our determination. First, the Commission stated that it was guided in its decision making by "the fundamental principle of cost causation 'that costs should be recovered in the rates of those customers who use the facilities and thus cause the cost to be incurred.'"<sup>33</sup> Based on the data supplied by ED3, the Commission found that the APS customers were not driving the need for the bulk of the upgrades and additions to the ED3 system and concluded, in accordance with the fundamental principle of cost causation, that "APS customers should not bear the burden of paying for distribution lines that serve only ED3 customers and provide no system-wide benefit."<sup>34</sup> In addition, the Commission does not permit the roll-in of costs associated with non-integrated facilities.<sup>35</sup> Thus, ED3 had the burden of first showing that its 12 kV distribution facilities are integrated. The data provided by ED3 did not provide evidence sufficient to demonstrate that the 12 kV facilities are integrated, however, so the Commission could not approve rolled-in pricing for those facilities.

18. We likewise reject ED3's claim that our denial of rolled-in treatment of the 12 kV distribution facilities is difficult to reconcile with Commission precedent establishing that "any degree of integration" is sufficient to justify rolled-in treatment. The precedent cited by ED3 addresses transmission, not distribution, facilities and is, therefore, not applicable. In addition, the Commission found, based on the evidence submitted by ED3, that its 12 kV facilities are distribution facilities that are not part of an integrated transmission network. Therefore, the "any degree of integration" principle is irrelevant. Moreover, to the extent that ED3 is arguing that the Commission's finding of no integration of the 12 kV facilities is the result of misunderstanding ED3's ten-year transmission plan, we find that ED3's reliance on our interpretation of the ten-year transmission plan is misplaced. ED3 had the burden of demonstrating that its proposed formula rate is just and reasonable. Therefore, even if the Commission had taken ED3's description of its transmission system out of context, such a misunderstanding would not overcome ED3's failure to meet its burden. Moreover, the ten-year transmission plan

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<sup>33</sup> May 17, 2010 Order, 131 FERC ¶ 61,143 at P 48 (quoting *Northern States Power Co.*, 64 FERC ¶ 61,324, at 63,379 (1993), *reh'g denied*, 74 FERC ¶ 61,106 (1996)).

<sup>34</sup> May 17, 2010 Order, 131 FERC ¶ 61,143 at P 47.

<sup>35</sup> See, e.g., *Southern Co. Servs., Inc.*, 116 FERC ¶ 61,247, at P 20 (2006).

was not the only evidence considered by the Commission. In reaching our determination, the Commission requested from ED3 and considered its documentation, but found no evidence to justify rolled-in pricing for all of ED3's 12 kV facilities.<sup>36</sup>

19. Equally misplaced is ED3's argument that the scope of transmission service originally ordered by the Commission should dictate the result in this case. In the 2002 Proposed and Final Orders, as ED3 correctly states, the Commission directed ED3 to provide transmission service of the same nature that ED3 was voluntarily providing.<sup>37</sup> However, the fact that ED3 provides APS with network, as opposed to point-to-point, transmission service has no bearing on the question of whether all of ED3's 12 kV facilities are integrated network transmission facilities for purposes of rolling in their costs and including them in a single rolled-in rate (as opposed to developing a separate, secondary distribution charge). Thus, the Commission's directive to ED3 to develop a secondary distribution charge for the specified 12 kV facilities does not conflict, either in logic or in practice, with ED3's service obligations under the 2002 Proposed and Final Orders.

20. We also reject ED3's assertion that the Commission enhanced ED3's burden of proof by requesting power flow studies and finding, in the absence of power flow studies, that the 12 kV facilities are not appropriate for rolled-in treatment. The Commission did not enhance ED3's burden by requesting power flow studies; as discussed above, ED3 had the burden of demonstrating the justness and reasonableness of its proposed formula rate and, therefore, had the burden of producing sufficient evidence to support its claims of integration. Power flow studies fall squarely within the range of evidence that ED3 could be expected to provide to satisfy its burden of persuasion, given the nature of its request, and the power flow studies were requested to assist the Commission in its analysis of the degree of integration of the ED3 transmission and distribution systems.<sup>38</sup> For example, detailed power flow studies depicting normal and contingency states of transmission systems would have been a valuable tool in understanding the topology and use of the system.

21. However, notwithstanding that ED3 had numerous opportunities to provide this information – in its pre-technical conference submittal, at the technical conference, or in

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<sup>36</sup> For example, the Commission reviewed numerous system maps and one-line diagrams, but did not have the benefit of power flow studies to evaluate the topology and use of the 12 kV facilities.

<sup>37</sup> 2002 Proposed Order, 98 FERC at 61,115; 2002 Final Order, 100 FERC ¶ 61,146 at P 7.

<sup>38</sup> Technical Conference Notice at 2.

either of the two rounds of post-technical conference briefings – ED3 chose to make its case without the benefit of power flow studies.<sup>39</sup> Without the benefit of power flow studies indicating the impact of power flow changes on ED3's 69 kV and 12 kV systems, there is insufficient evidence to support ED3's characterization that its 12 kV distribution system is integrated.

22. In addition, contrary to ED3's claims, the Commission has not allowed rolled-in treatment of facilities exhibiting the same characteristics as the ED3 12 kV distribution system. Rather, as discussed above, ED3 erroneously overlooks the distinction, for ratemaking purposes, between distribution and transmission; the Commission generally allows the direct assignment of Commission-jurisdictional distribution facilities.<sup>40</sup> As discussed below, none of the cases cited by ED3 support ED3's claim that the Commission should permit the roll-in of its low voltage distribution facilities.

23. In *Allegheny*, the applicant specified, and the Commission was therefore able to analyze, 18 discrete delivery points.<sup>41</sup> In contrast, as we found in the May 17, 2010 Order, ED3 made no attempt to identify specific facilities for rolled-in treatment. In fact, ED3 asked the Commission to allow it to roll-in the costs of its entire distribution system, down to the level of individual household meter connections, and did not limit its request to specific points of delivery in the distribution system.<sup>42</sup> *Boston Edison* dealt with subtransmission facilities, and not distribution facilities. Moreover, in *Boston Edison*, the Commission disallowed system-average pricing as a cost allocation methodology for the subtransmission facilities at issue and rejected a proposal to roll in the cost of a transformer and associated facilities that were not used to serve the customer.<sup>43</sup> Additionally, other than its naked assertion that the facilities in the cited cases exhibit the

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<sup>39</sup> For example, in response to the Commission's request for power flow studies in the Technical Conference Notice, ED3 merely referred the Commission to previously submitted evidence. ED3 November 9, 2009 Technical Conference Submittal at 9. However, upon review, the Commission found that the referenced document did not contain power flow studies.

<sup>40</sup> See, e.g., *Tex-La*, 69 FERC at 62,036.

<sup>41</sup> *Allegheny*, 122 FERC ¶ 61,160 at P 3; see also May 17, 2010 Order, 131 FERC ¶ 61,134 at P 45.

<sup>42</sup> May 17, 2010 Order, 131 FERC ¶ 61,134 at P 45.

<sup>43</sup> *Boston Edison*, 61 FERC ¶ 61,026 at 61,141. The rejection of the proposed system-average cost methodology was not raised on exceptions to the initial decision, and the Commission affirmed without further discussion.

same characteristics or serve loads “in exactly the same way” as the ED3 distribution system, ED3 provides no support for its comparison.

24. We also disagree with ED3’s assertion that it has demonstrated that its 12 kV facilities provide system-wide reliability benefits. ED3 has simply not demonstrated that all of its 12 kV facilities provide system-wide “backup” to other 12 kV or 69 kV lines; rather, the evidence presented by ED3 indicates that the primary function of the 12 kV distribution lines is to deliver power from the transmission system, i.e., to deliver power to customers locally. Any backup provided to other 12 kV or 69 kV lines appears to be equally local in nature and, absent a demonstration that was not presented here, would not be expected to provide system-wide benefits. On rehearing, ED3 provides a definition of a backup line,<sup>44</sup> and cites *Allegheny* and *Northeast Texas Elec. Coop.*, arguing that the Commission found in those cases that subtransmission facilities provided a system-wide reliability benefit. ED3 does not, however, explain how its 12 kV facilities meet the criteria set forth in those orders. First, in both cases, the Commission assessed the appropriateness of rolling in the costs of transmission and subtransmission facilities, and did not consider the roll-in of low voltage distribution facilities. Moreover, without power flow studies, it is unclear what facilities are affected by outages on other lines. The mere presence of multiple connections and various switching arrangements on those distribution facilities does not, by itself, demonstrate a system-wide reliability benefit. Rather, the primary benefit of the switching features of the distribution system appears to be the isolation of local areas for maintenance or repairs under contingency conditions.

25. It is unclear from ED3’s rehearing request how the approach taken by the Commission in *Allegheny* supports ED3’s claim that all of the 12 kV facilities proposed for inclusion in the formula rate provide backup or other system-wide reliability benefits. *Allegheny* does not address the question of whether contingency switching arrangements are sufficient to demonstrate integration of distribution facilities. Moreover, in *Allegheny*, the Commission found that each of the 13 delivery points for which rolled-in treatment was approved had more than one subtransmission line transporting electricity to it and that each subtransmission line provides backup to another subtransmission line.<sup>45</sup> Unlike the situation in *Allegheny*, the Commission was not able to focus its evaluation of the ED3 transmission and distribution systems on discrete delivery points. Without clear points of reference, the Commission had no choice but to focus on the configuration of the 12 kV facilities to determine whether APS customers receive any benefit from the 12 kV facilities that do not directly serve APS load. Based on our

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<sup>44</sup> ED3 states that a backup line is “an additional electric path or loop line that provides support and reliability to other lines.” ED3 Rehearing Request at 12 (citing *Allegheny*, 122 FERC ¶ 61,160 at P 29 n.30).

<sup>45</sup> *Allegheny*, 122 FERC ¶ 61,160 at P 29.

review of the system maps and one-line diagrams provided by ED3, we found that the 12 kV facilities that do not directly serve APS load do not provide backup and do not provide system-wide reliability benefits.

26. In addition, in *Sierra Pacific*, another of the cases cited by ED3 to support its claim that its 12 kV facilities provide backup capability, the switching arrangements at issue involved the automatic rerouting of power throughout a looped subtransmission system. The ED3 facilities at issue are distribution facilities, not subtransmission facilities like the facilities at issue in *Sierra Pacific*. Thus, we find that ED3 misapplies the relevant precedent regarding what constitutes “backup.”

27. Finally, while we agree with ED3 in principle that transmission customer loads need not be disbursed uniformly throughout a system to justify a rolled-in rate, the principle of cost causation does not require approval of the roll-in of the costs of ED3’s entire 12 kV distribution system. The Commission’s denial of rolled-in treatment of the 12 kV facilities is not a matter of quantifying benefits. Rather, it is a matter of assigning costs in a manner that reflects the true cost-drivers. Based on the facts and circumstances presented in this case, the rate that ED3 charges APS for service over its distribution facilities should be based on the costs of those distribution facilities that are actually used to serve APS customers. ED3 has not offered any justification in its rehearing request to convince us that the APS customer load is driving the need for the expansions and upgrades that have resulted in ED3 applying to increase the rate it charges APS. We add that, in the May 17, 2010 Order, the Commission permitted ED3 to recover the costs of those 12 kV facilities that actually serve APS customers via the secondary distribution charge; for the reasons discussed in that order and above, the Commission found and continues to find that direct assignment, and not rolled-in pricing, is the proper method of cost recovery. We continue to find that, because APS load is so widely dispersed and because the APS load is not growing, it would not be just and reasonable to permit ED3 to roll the costs of these expansions and upgrades into its system average formula rate.

### C. CWIP

28. We will deny rehearing on the issue of ED3’s proposal to include 100 percent of CWIP in its formula rate. In its rehearing request, ED3 appears to conflate questions regarding the rationale underlying the Commission’s 50 percent CWIP limitation<sup>46</sup> with the issue of whether ED3 has made the showing required for recovery of 100 percent of CWIP. ED3 reiterates that, because it has no stockholders, it is not susceptible to the same potential for institutional conflict that ED3 claims to have motivated the 50 percent limitation. However, ED3 offers no evidence as to why this claimed lack of institutional conflict supersedes the showing required by Order No. 679 or why it should guarantee

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<sup>46</sup> This limitation is set forth in 18 C.F.R. § 35.25 (2010) (CWIP Regulation).

100 percent CWIP recovery. As we explained in the May 17, 2010 Order, Order No. 679 is the most appropriate framework for evaluating this type of transmission incentive request.<sup>47</sup> Because we found that ED3 had not made the showing required by Order No. 679, we denied ED3's request for inclusion of 100 percent of CWIP.<sup>48</sup> ED3 has not provided any persuasive reason on rehearing to persuade us that Order No. 679 is not an appropriate analytical framework or that ED3 meets the Order No. 679 criteria. Thus, we continue to find that the claimed lack of "institutional conflict" between ED3 and its retail customers is irrelevant to our analysis.<sup>49</sup>

29. Finally, we note that the method used by ED3 to allocate the cost of service to its own retail customers does not dictate the Commission's determination of whether the rates charged by ED3 to APS for providing Commission-jurisdictional transmission service are just and reasonable.<sup>50</sup> Therefore, ED3's inclusion of 100 percent of CWIP in its retail rates does not supersede the Commission's duty to apply the relevant statutes and regulations in our evaluation of ED3's request. Likewise, nothing in section 212 of the FPA<sup>51</sup> requires the Commission to grant transmission incentives absent the required showing. Thus, we continue to disagree with ED3's contention that section 212 of the FPA requires the Commission to approve a rate structure for Commission-jurisdictional service that is identical to the rate ED3 sets for its retail service.

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<sup>47</sup> May 17, 2010 Order, 131 FERC ¶ 61,143 at P 56.

<sup>48</sup> *Id.* P 56, 58. The Commission noted that ED3 has not demonstrated that it faces any particular risks or challenges, such as a weakened financial condition or inadequate cash flows, and that instead it appeared that ED3's expansion projects would go forward regardless of whether 100 percent CWIP is included in its formula rate.

<sup>49</sup> It is not unreasonable for the Commission to adhere to its standard approach; the applicant has the burden of demonstrating why it would be just and reasonable for the Commission to deviate from its general policy. *Westar Energy, Inc. v. FERC*, 568 F.3d 985, 989 (D.C. Cir. 2009).

<sup>50</sup> It is well established that the Commission is not bound by a state commission's ratemaking decision. *See, e.g., Public Service Company of Indiana, Inc. v. FERC*, 575 F.2d 1204, 1218, 1219 (7th Cir. 1978); *San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary Servs.*, 127 FERC ¶ 61,269, at P 209 (2009); *Barton Village, Inc. v. Citizens Utils. Co.*, 98 FERC ¶ 61,325, at P 12 (2002); *Florida Power & Light Co.*, 98 FERC ¶ 61,325, at P 16 (2002).

<sup>51</sup> 16 U.S.C. § 824k (2006).

**D. Cost of Service Data**

30. The Commission will deny ED3's request for rehearing or clarification on the question of whether it must use facility-specific cost of service data to develop the secondary distribution charge required by the May 17, 2010 Order. The result in *Allegheny*, where the Commission permitted the use of average system costs in lieu of facility-specific costs, was a fact-driven departure from Commission precedent on the proper method for directly assigning costs because the facility-specific cost of service data did not exist,<sup>52</sup> a "unique result" that was not intended "to provide a template for future cases."<sup>53</sup> The Commission also reaffirmed its "long standing requirement" that direct assignment charges must be based on facility-specific data.<sup>54</sup>

31. As the result of a recent ruling by the Arizona Corporation Commission (Arizona Commission), all of APS's customers within the ED3 footprint will be transferred to ED3.<sup>55</sup> The impact of this ruling on this case is two-fold. First, because all of the APS customers within the ED3 service area will be transferred to ED3, the section 211 transmission service provided by ED3 to APS, along with the associated rates, will impact very few APS customers on an ongoing basis. Thus, the primary effect of applying the rolled-in formula rate and secondary distribution charges required by the May 17, 2010 Order will be to establish the amount of the refund due from ED3 to APS for the period from July 16, 2008, when the ED3 formula rate became effective, up until the effective date of the revised, two-tiered rate. Second, the Arizona Commission Decision provides APS with the necessary authority to provide the facility-specific data to ED3.<sup>56</sup> Accordingly, our understanding is that APS will provide the necessary facility-

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<sup>52</sup> *Allegheny*, 122 FERC ¶ 61,160 at P 34.

<sup>53</sup> *Id.* P 35.

<sup>54</sup> *Id.* The Commission also stated, "We emphasize that, in this order, we are approving a rate methodology, and not specific rates, which Allegheny Power is to submit in a future compliance filing. We thus will have an opportunity to determine whether the actual rates reflecting the use of average costs for direct assignment are just and reasonable." *Id.*

<sup>55</sup> Arizona Commission Decision No. 71714, Docket No. E-01345A-08-0426 (June 3, 2010) (Arizona Commission Decision).

<sup>56</sup> *Id.* at P 102.

specific cost of service data to ED3.<sup>57</sup> ED3 should be able to use this data to comply with the Commission's directive in the May 17, 2010 Order regarding the development of the secondary distribution charge.<sup>58</sup> In the event that the necessary data for all of the eligible facilities identified in Appendix A of the May 17, 2010 Order does not exist, the Commission will permit ED3 to use data from facilities that are substantially comparable to the facilities at issue.

The Commission orders:

ED3's request for rehearing and/or clarification is hereby denied, as discussed in the body of this order.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.

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<sup>57</sup> See ED3 July 1, 2010 Expedited Motion to Defer Compliance Filing in Docket No. TX02-1-003 at 2 (explaining that ED3 expects to receive the data from APS in mid-September).

<sup>58</sup> We note that, in developing the secondary distribution charge, ED3 may only include the 12 kV facilities identified in Appendix A of the May 17, 2010 Order as eligible for recovery. Furthermore, ED3 must identify the plant cost, depreciation, operation and maintenance cost, depreciation expense, and return component in developing this charge. In addition, ED3 must address the issue of account balances for Accounts 369 (Services), 370 (Meters), and 373 (street lighting and traffic signals) in the context of the secondary distribution charge, consistent with the facilities listed in Appendix A.