

133 FERC ¶ 61,154
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.

Startrans IO, L.L.C.

Docket No. ER08-413-002

ORDER DENYING REHEARING

(Issued November 18, 2010)

1. This order addresses the request for rehearing filed by the California investor owned utilities (California Utilities)¹ regarding the Commission's March 31, 2008 order² in the above-captioned proceeding. We affirm the March 2008 Order's conclusion that it was appropriate for Startrans IO, L.L.C. (Startrans) to use a regional proxy group in calculating its proposed return on equity (ROE) of 13.5 percent; however, we clarify that we are not mandating the use of regional proxy groups in this or in other cases. We also clarify that our decision to make an up-front ROE determination will depend on the facts and circumstances of individual cases.³

I. Background

2. Startrans, a transmission-only limited liability company, entered into an agreement with the City of Vernon, California (Vernon), a non-jurisdictional municipality and a Participating Transmission Owner within the California Independent System Operator Corporation (CAISO), to acquire Vernon's ownership interests in two transmission line projects: (1) the Mead-Adelanto Project; and (2) the Mead-Phoenix Project (collectively, Mead Transmission Interests or Mead Facilities).

¹ California Utilities consist of: Pacific Gas & Electric Company, San Diego Gas & Electric Company, and Southern California Edison Company.

² *Startrans IO, L.L.C.*, 122 FERC ¶ 61,306 (2008) (March 2008 Order).

³ For purposes of this order, up-front ROE determinations include those situations in which the Commission makes ROE determinations following a paper hearing process, as well as situations in which the ROE determination is made on the basis of a review of a party's filing and any protests.

3. On January 4, 2008, Startrans filed the proposed tariff and associated Transmission Revenue Requirement to establish itself as a new Participating Transmission Owner within the CAISO, pursuant to section 205 of the Federal Power Act.⁴ In addition, Startrans requested certain rate incentives, including an incentive ROE, an acquisition adjustment of approximately \$31.7 million, and 100 percent construction work in progress, pursuant to Order No. 679.⁵ Startrans proposed an ROE of 13.5 percent, and applied a proxy group comprising a nationwide group of companies that Startrans asserted had comparable risk. Commission Staff subsequently issued a deficiency letter that directed Startrans either to use a regional proxy group of companies located in the Western Electricity Coordinating Council (WECC), consistent with the Commission's order in *Atlantic Path 15, LLC*,⁶ or to provide the Commission with additional information about the national proxy group that it had applied in its filing. On February 7, 2008, Startrans filed its response to the deficiency letter, opting to use the WECC-wide regional proxy group, but Startrans still requested an ROE of 13.5 percent, which it argued was reasonable under its new calculation.

4. The March 2008 Order accepted Startrans' proposed ROE, finding that it was appropriate for Startrans to use a regional proxy group, consistent with *Atlantic Path 15* and other Commission orders, and explained that geographic location was a relevant factor in identifying companies of comparable risk.⁷

5. California Utilities filed a request for rehearing of the March 2008 Order, arguing that the Commission erred in adopting a policy that requires applicants in the western United States to use a WECC-wide regional proxy group in calculating requested ROEs.

⁴ 16 U.S.C. § 824d (2006).

⁵ *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).

⁶ 122 FERC ¶ 61,135 (2008) (*Atlantic Path 15*).

⁷ The March 2008 Order also rejected Startrans' request for an acquisition adjustment and for 100 percent construction work in progress. Startrans sought rehearing on these issues. Pursuant to the terms of a Commission-approved settlement, Startrans withdrew its request for rehearing on the denial of the construction work in progress but retained its rehearing request with respect to the denial of the acquisition premium. *See Startrans IO, L.L.C.*, 128 FERC ¶ 61,118 (2009). On March 18, 2010, the Commission issued an order denying Startrans' request for rehearing on this issue. *Startrans IO, L.L.C.*, 130 FERC ¶ 61,209 (2010).

California Utilities also argued that the Commission did not need to make up-front ROE determinations in all cases.

II. Discussion

A. Regional Proxy Groups

1. Rehearing Request

6. California Utilities assert that the Commission should not require Startrans or other western utilities to use a WECC-only proxy group. California Utilities note that the Commission's policy of using a proxy group comprising only entities located in the WECC was only first announced in *Atlantic Path 15*, which was issued less than two months before the March 2008 Order, and that this policy decision reversed decades of Commission precedent.

7. California Utilities explain that western utilities compete for capital in a national market, not a regional one, and although the WECC region may be electrically and commercially integrated, western utilities are diverse and have very different business models. California Utilities note that most WECC members do not belong to a Regional Transmission Organization (RTO) or an Independent System Operator (ISO), and that WECC itself is primarily a reliability organization for western utilities. California Utilities argue that the Commission's goal of simplifying ROE cases for western utilities is just as well served by using a national sample of utilities rather than a region-wide one. California Utilities contend that a utility that is willing to undergo the scrutiny of a hearing should have the flexibility of being able to develop a proxy group that is appropriate for its specific circumstances. California Utilities state that a one-size-fits-all approach would limit the Commission's ability to develop appropriate criteria tailored to an individual case.⁸

8. California Utilities note that the Commission has cited to precedent involving utilities in New England⁹ and the Midwest¹⁰ in support of the policy expressed in *Atlantic Path 15* that a region-wide proxy group should be used. However, California Utilities assert that these cases are distinguishable because they involved utilities that were part of the same ISO or RTO. Moreover, California Utilities explain that since the issuance of *Bangor Hydro* and *Midwest ISO*, both PG&E and SDG&E have filed proposed ROEs using a national sample to determine the appropriate proxy groups, and

⁸ California Utilities Rehearing Request at 9.

⁹ *Bangor Hydro Electric Co.*, 117 FERC ¶ 61,129 (2006).

¹⁰ *Midwest Indep. Transmission Sys. Operator, Inc.*, 100 FERC ¶ 61,087 (2002).

the Commission orders on those filings did not indicate that a regional proxy group must be used or that it would extend the holdings of those cases applying an RTO-wide proxy group to western utilities, most of which were not RTO or ISO members.¹¹ California Utilities state that they do not necessarily object to the use of an RTO-wide proxy group in the appropriate case; however, they argue that the Commission has not explained why being located in the WECC region is an appropriate measure of risk.

9. California Utilities assert that, while a proxy group should include those companies that face similar risks as those faced by the applicant, western utilities operate under vastly different market structures from each other and rely on different portfolios of power supply resources. California Utilities note that the climate in the WECC region is very diverse, and thus a utility in southern California faces very different climate-related risks from those faced by a utility in Idaho. California Utilities also contend that there is no record evidence that investors perceive geography as a factor when differentiating between otherwise comparable utilities.

10. Citing *Consumers Energy Company*,¹² California Utilities assert that the Commission has departed from prior policy without a rational explanation. In *Consumers*, the Commission reversed an Administrative Law Judge's determination that a utility located in another part of the country should be excluded from a proxy group, stating that "the judge should not have eliminated [the out-of-area utility] as a proxy choice solely because of geographical or climatic differences."¹³

11. California Utilities believe that limiting the proxy group to utilities in the WECC region ignores the fact that western utilities compete for scarce capital with other companies in the nation; that is, the financial markets in which that competition occurs are not regional, but national or international in scope. According to California Utilities, even if geography were a factor to some investors, it would be less important than other factors that the Commission traditionally has looked to in developing proxy groups.¹⁴

12. Further, California Utilities state that the Commission has not addressed the far-reaching and long-term impacts of a new proxy group policy on future ROE

¹¹ California Utilities Rehearing Request at 12-13 (*citing Pacific Gas and Elec. Co.*, 120 FERC ¶ 61,296 (2007) and *San Diego Gas & Elec. Co.*, 118 FERC ¶ 61,073 (2007)).

¹² 98 FERC ¶ 61,333 (2002) (*Consumers*).

¹³ *Id.* at 62,412.

¹⁴ California Utilities Rehearing Request at 17.

determinations. California Utilities contend that if utilities outside of the WECC region are excluded from the proxy group for a western utility, then both the top and the midpoint of the range of reasonableness will be lower.¹⁵

13. California Utilities further argue that adopting a WECC-only proxy group will not provide additional regulatory certainty, explaining that use of a national sample, with the same appropriate screens, provide just as much certainty. California Utilities also contend that use of a national proxy group would satisfy Commission policy goals, be more efficient than use of a regional proxy group, and consistent with precedent.¹⁶

2. Commission Determination

14. In a concurrently issued order on rehearing in the *Atlantic Path 15* proceeding, we clarify our policy on proxy group composition.¹⁷ As explained in that order, the Commission's obligation is to ensure that a filing company's proxy group consists of companies with comparable risks to those facing the applicant.¹⁸ While geographic proximity may be a relevant factor in identifying companies with comparable risks, it is not the sole basis for inclusion of companies in a proxy group. Thus, the Commission will not mandate that a proxy group must be composed of companies in the same geographic region as the filing company.

15. Elaborating on this point, we also note in today's *Atlantic Path 15* rehearing order:

The question of which companies should be included in a proxy group is properly resolved based on the facts and circumstances of each case. In some cases, a filing company may rely solely on companies in its region to form a proxy group and to perform its DCF analysis, after demonstrating that these companies have comparable risk to the filing company. In other cases, a filing company may identify companies with comparable risk by looking beyond its geographic region. The filing company must, of course, fully support

¹⁵ For example, California Utilities state that, in this proceeding, the range of reasonableness using a WECC-only sample was between 7.63 percent and 13.67 percent. In contrast, if a national sample were used, the range of reasonableness would be between 8.75 percent and 13.67 percent.

¹⁶ California Utilities Rehearing Request at 19-20.

¹⁷ *Atlantic Path 15, LLC*, 133 FERC ¶ 61,153 (2010).

¹⁸ *See id.* P 13.

its choice of a proxy group, and intervenors are free to challenge the reasonableness of the filing company's choice.¹⁹

16. Here, California Utilities argue that the Commission should not require that Startrans or other western utilities use a proxy group comprising only companies located in the WECC. However, California Utilities do not squarely object to Startrans' use of a regional proxy group. Instead, California Utilities' objection to the March 2008 Order is grounded in what it perceives as a change in the Commission's policy, starting with *Atlantic Path 15*, indicating a preference for regional proxy groups. As discussed above, we clarify that the Commission's focus is on whether a proxy group includes companies of comparable business or financial risk, and we will not mandate that a proxy group must be composed of companies in the same geographic region as the filing company.

17. Moreover, we note that in this case we did not mandate that Startrans use a regional proxy group; rather, in the deficiency letter issued to Startrans, Commission Staff directed Startrans either to apply a regional proxy group or file additional information supporting its proposed national proxy group.²⁰ Although it could have attempted to support its proposed national proxy group, Startrans chose to use a proxy group comprised of companies located within the WECC footprint. The March 2008 Order itself stated that Startrans' use of a regional proxy group, consistent with *Atlantic Path 15* and other cases, was "appropriate" and that "being located in the same geographic and economic region is relevant in determining whether companies face similar business risk."²¹ In the March 2008 Order, we were looking at the facts and circumstances that were squarely before us, i.e., Startrans' use of a regional proxy group. We reaffirm here that Startrans provided adequate support for using a proxy group comprised of entities located within the WECC footprint.

18. Because we clarify our policy, as discussed herein, California Utilities' request for rehearing is denied.

¹⁹ *Id.* P 14.

²⁰ See Deficiency Letter, Docket No. ER08-413-000, *et al.*, at 2-3 (Feb. 22, 2008) (directing Startrans either to provide additional information regarding its proposed national proxy group, such as providing corporate credit information for the proxy companies and incorporating the Commission's growth rate for each company, or adopt a proxy group comprising entities in the WECC).

²¹ March 2008 Order, 122 FERC ¶ 61,306 at P 25.

B. Up-Front ROE Determination

1. Rehearing Request

19. California Utilities argue that the Commission should not require up-front ROE determinations in all cases, stating that while regulatory certainty and prompt resolution may support the use of an up-front ROE determination in some circumstances, mandating the approach for all ROE cases (particularly general rate cases) is inappropriate. First, California Utilities explain that the considerations that may counsel for up-front ROE determinations in incentive rate cases (e.g., up-front decisions may help with financing projects) may not be present in general rate cases, which are more likely to be set for hearing to address other issues.

20. Second, California Utilities contend that a general rate case applicant that is willing to go to hearing should have the flexibility to develop a proxy group that is the most appropriate under the circumstances. Third, California Utilities argue that general rate cases require a more tailored analysis than incentive rate cases, because the focus in general rate cases is establishing a range of reasonable returns and placing the applicant's ROE at an appropriate point in that range, while the focus in an incentive rate case is to ensure the applicant is not above the top of the range of reasonable returns. California Utilities assert that this approach is consistent with Commission precedent.²²

2. Commission Determination

21. In response to California Utilities' argument that we should not require an up-front ROE determination in all cases, we clarify that our decision to make an up-front ROE determination will depend on the facts and circumstances of each individual case.

22. While we note that in *Atlantic Path 15*, we acknowledged that use of regional proxy groups may allow for up-front ROE determinations, we recognize that choosing a regional proxy group is not independently dispositive. We will look at the facts and circumstances presented in each proceeding, including the written submissions of the filing company and intervenors in determining whether it is appropriate to make an up-front ROE determination or to order an evidentiary hearing.

23. Nonetheless, we affirm that the Commission retains discretion to make up-front ROE determinations if the record before it is sufficient to make such a summary finding. Recently, in *Pioneer Transmission LLC*,²³ the Commission rejected the claim that it must always order trial-type hearings in ROE cases. As the Commission noted in *Pioneer*,

²² California Utilities Rehearing Request at 22.

²³ 130 FERC ¶ 61,044 (2010) (*Pioneer*).

federal courts have held that a formal trial-type hearing is unnecessary where there are no material facts in dispute.²⁴ The Commission further emphasized that it is not sufficient for a protesting party merely to allege an issue of disputed fact—parties “must make an adequate proffer of evidence to support them.”²⁵ The *Pioneer* order emphasized, “The Commission is only required to provide a trial-type hearing if the material facts in dispute cannot be resolved on the basis of written submissions in the record.”²⁶

24. The same principles that the Commission articulated in *Pioneer* may also be applied to general rate cases. If we are able to make summary determinations based on the written record, then we are not required to establish trial-type evidentiary hearing procedures. If intervenors believe that a trial-type hearing is more appropriate than an up-front ROE determination in general rate cases or incentive rate cases, we will consider such arguments on a case-by-case basis. Likewise, where filing companies themselves request that the Commission establish hearing procedures, we will consider those requests as well.

25. In light of this clarification with respect to the Commission’s approach to making up-front ROE determinations, we deny California Utilities’ request for rehearing regarding that issue.

The Commission orders:

California Utilities’ request for rehearing is hereby denied, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

²⁴ *Id.* P 35 (citing *Moreau v. FERC*, 982 F.2d 556, 568 (D.C. Cir. 1993)). See also, e.g., *Blumenthal v. FERC*, 613 F.3d 1142, 1144 (D.C. Cir. 2010).

²⁵ *Pioneer*, 130 FERC ¶ 61,044 at P 35 (quoting *Cerro Wire & Cable Co. v. FERC*, 677 F.2d 124, 129 (D.C. Cir. 1982)).

²⁶ *Id.* n.73.