Federal Energy Regulatory Commission
July 20, 2006
Open Commission Meeting
Discussion Item E-3, E-4 & E-15

Good Morning Mr. Chairman and Commissioners. My name is Jeff Hitchings from the Office of Energy Markets and Reliability. Seated next to me is Andre Goodson from the Office of General Counsel. Other team members that worked on this rule are Sebastian Tiger from the Office of Enforcement, and Tina Ham, Martin Kirkwood, and Kimberly Bose from the Office of General Counsel. The team members on E-4 and E-15 are also seated at the table and will be making a presentation on those items.

E-3 is a draft Final Rule that Promotes Transmission Investment with Pricing Reform, pursuant to the requirements of the Transmission Infrastructure Investment provisions in section 1241 of the Energy Policy Act of 2005, which adds a new section 219 to the Federal Power Act. The draft Final Rule facilitates needed investment that will ensure reliability and reduce the consumer cost of power by reducing transmission congestion. The need for transmission investment is urgent. Investment in transmission has dropped significantly in real dollar terms over the past 30 years while electricity load using the grid more that doubled and congestion costs remain significant in a number of markets. By adopting the provisions of the November 2005 proposed rulemaking, this draft Final Rule will promote increased capital investment by providing greater regulatory certainty and procedural flexibility for applicants making transmission investments.

The draft Final Rule identifies specific incentives that the Commission will allow when justified in the context of individual declaratory orders or filings by Public Utilities under section 205 of the Federal Power Act. The draft Final Rule permits an application to tailor its proposed incentives to the type of transmission investments being made and the applicant is required to demonstrate that its proposal ensures reliability or reduces the cost of delivered power to customers by reducing transmission congestion, as required by the Energy Policy Act of 2005. The Commission will permit incentives only if the incentive package as a whole results in a just and reasonable rate.

The draft Final Rule provides procedural flexibility, including the use of expedited declaratory orders on permitted ratemaking treatments, to help with financing and up-front regulatory certainty for project investments.

As well, the Draft Final Rule makes clear that not every incentive identified herein will be necessary or appropriate for every new transmission investment and approval of such incentives will be evaluated on a case-by-case basis.

Today's draft Final Rule adopts a number of price reforms including:

- incentive rate of return on equity for new investment by public utilities (both traditional utilities and transcos)
- full recovery of prudently incurred construction work in progress
- full recovery of prudently incurred pre-operations costs
- full recovery of prudently incurred costs of abandoned facilities
- use of hypothetical capital structures
- accumulated deferred income taxes for transcos
- adjustments to book value for transco sales/purchases
- accelerated depreciation
- deferred cost recovery for utilities with retail rate freezes

- A higher rate of return on equity for utilities that join transmission organizations, such as (but no necessarily limited to) RTOs or ISOs.

In addition, the draft Final Rule provides cost recovery of prudently incurred costs necessary to comply with mandatory reliability standards and prudently incurred costs related to infrastructure development in national interest transmission corridors. The draft Final Rule also requires public utilities that are granted incentives to file an annual reporting requirement, FERC-730, to allow the Commission to track investment and project resources and reasons for project delays.

Next staff will present two other draft orders, E-4 and E-15. These draft orders seek to apply the principles set forth in the draft Final Rule to proposals for transmission incentives on a case-by-case basis. First Roshini Thayaparan will give a brief presentation on E-4, followed by Rachel Spiker's presentation on E-15.

Good morning/afternoon. My name is Roshini Thayaparan. Seated next to me is Kurt Longo. Other team members that worked on item E-4 are Kimberly Bose, Andre Goodson, Kevin Huyler, Tatyana Kramskaya, and Daniel Nowak.

The draft order grants the four incentives requested by Allegheny Energy, Inc. and its subsidiaries, Monongahela Power Company, Potomac Edison Company, and West Penn Power Company. Allegheny proposes to construct a 500-kilovolt transmission line within the PJM region. As amended by the Regional Transmission Expansion Plan review released by PJM in June, the proposed line would extend from southwestern Pennsylvania to Virginia. The project has a targeted completion date of 2011. Preliminary cost estimates for Allegheny's portion of the project and other upgrades are approximately $820 million.

The draft order approves the four transmission incentives sought by petitioners. The draft order grants the petition for declaratory order approving the incentive rates proposed by Allegheny for the proposed Project pursuant to our existing authority under FPA section 205, and consistent with Congress' direction in new FPA section 219. The approved incentives include: (1) a return on equity set at the high end of the zone of reasonableness, (2) the option to timely recover the cost of capital associated with Construction Work In Progress; (3) the ability to expense and recover, on a current basis, pre-construction and pre-operating costs; and (4) the option to recover all prudently incurred development and construction costs if the project is abandoned as a result of factors beyond the petitioners' control. The draft order also approves certain accounting authority for the deferral for future recovery of such costs not yet being recovered plus related carrying costs.

Next, Rachel Spiker will give a presentation on E-15.

Good morning/afternoon. My name is Rachel Spiker. Seated next to me is Moon Paul. Other team members that worked on item E-15 are Jignasa Gadani, Daniel Nowak, Tatyana Kramskaya, Kevin Huyler, and Sebastian Tiger.

E-15 conditionally approves the three incentive rates requested by AEP, for a proposed, new 765-kilovolt, 550-mile transmission line that would extend from west to east across the PJM region, from West Virginia to New Jersey. AEP estimates that the proposed Project and associated facilities will cost $3 billion to construct and take 8 years to complete.

The draft order grants the petition for declaratory order approving the incentive rates proposed by AEP for the proposed Project pursuant to our existing authority under FPA section 205, and consistent with Congress' direction in new FPA section 219, on the condition that the proposed Project is included as part of the PJM Regional Transmission Expansion Plan. The approved incentives include: (1) a return on equity set at the high end of the zone of reasonableness; (2) the option to timely recover the cost of capital associated with construction work in progress; and (3) the ability to expense and recover on a current basis the costs AEP incurs during the pre-construction and pre-operating period. The draft order conditions approval of these incentives on inclusion of AEP's proposed project in PJM's Regional Transmission Expansion Plan.

This concludes our joint presentation. We are pleased to answer any questions.