

137 FERC ¶ 61,119
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Public Service Company of New Mexico

Docket No. ER11-4534-000

ORDER ACCEPTING AND SUSPENDING PROPOSED RATES AND
ESTABLISHING HEARING AND SETTLEMENT JUDGE PROCEDURES

(Issued November 14, 2011)

1. On September 15, 2011, Public Service Company of New Mexico (PNM) filed with the Commission an unexecuted amended power sales agreement (Amended Agreement) between PNM and Navopache Electric Cooperative, Inc. (Navopache). As discussed below, we shall accept the filing, suspend it for a five-month period, to be effective April 14, 2012, subject to refund, and shall set all issues raised by the filing for hearing and settlement procedures, except those decided below.

I. Background

2. PNM is a New Mexico corporation owning or leasing approximately 3,170 circuit miles of electric transmission lines and 2,350 MW of generating facilities.¹ PNM provides capacity, energy, transmission services, and ancillary services to Navopache, a non-profit electric cooperative, under a 1999 power sales agreement (1999 Agreement). In 2009, the 1999 Agreement was amended to add a new section 9.4 requiring PNM and Navopache to negotiate a formula-based rate for wholesale power sales service to become effective after July 1, 2011.²

II. PNM's Filing

3. In its filing, PNM seeks to revise the rates established by a 2009 amendment to the 1999 Agreement. PNM states that it and Navopache were unable to reach agreement on such revised rates, and PNM was therefore compelled to file an unexecuted amended

¹ PNM Filing Letter at 2.

² *Id.* at 4.

power sales agreement with the Commission in this docket.³ In the Amended Agreement, PNM proposes a power charge of \$22.56 per kW-month and an energy charge of \$9.61 per MWh.⁴

4. PNM's proposed cost of service rate is based on an 11.0 percent rate of return on equity (ROE), which includes a 9.76 percent base ROE and a 124 basis point risk adder.⁵ PNM proposes to use the midpoint ROE from its stated zone of reasonableness instead of the median to form the base ROE. PNM contends that use of the midpoint ROE is appropriate because the Commission has stated that the median ROE is suitable for individual utilities facing average risk,⁶ but PNM contends that it faces higher than average business and financial risks.

5. PNM states that it has eliminated the high and low discounted cash flow (DCF) results from the zone of reasonableness, thus removing all outlying results and focusing on companies that form the central tendency of the proxy group. Thus, PNM argues that the results of its DCF analysis are balanced (i.e., the results are not skewed upward or downward) and that it is therefore appropriate to use the midpoint ROE in this case. PNM states that the 9.48 percent median ROE resulting from the DCF result for its proxy group is significantly lower than the average authorized ROE of 10.37 percent for retail electric utilities in 2010.

6. In addition to the proposed increases in charges for power and energy, PNM adds that Navopache's electric system is not physically interconnected with PNM transmission lines. Therefore, Navopache must have transmission rights across the transmission systems of Arizona Public Service Company (APS), Salt River Project (Salt River) and Tucson Electric Power Company (Tucson) to serve Navopache under the Amended Agreement.⁷ While PNM acknowledges that Navopache has acquired rights from

³ *Id.* at 5.

⁴ *Id.* at 5-6. PNM states that it incurs "power (capacity), energy production, and transmission costs in providing and delivering energy to Navopache under the terms of the Original PSA." The parties refer to the obligation to deliver "power and energy" throughout their filings. The new rates increase PNM's revenue from approximately \$21.85 million to \$30.55 million. PNM Ex. Nos. Period II, Statement BH, Line 17 and Period II, Statement BG, Line 19.

⁵ PNM argues that due to its below investment grade credit rating, it faces higher risk and requires a 124 basis point adder to attract investors. Hevert Test. at 43-44.

⁶ PNM cites *Golden Spread Electric Coop.*, 123 FERC ¶ 61,047 (2008).

⁷ Hevert Test. at 7.

Tucson and Salt River needed for service under the Amended Agreement, PNM acquired rights over the APS system to deliver power and energy under the Amended Agreement. PNM states that it entered into a network integration transmission service agreement with APS solely to serve Navopache under the Amended Agreement, and that it is therefore appropriate to directly assign all the costs under such agreement to Navopache. PNM proposes to do so in the Amended Agreement.⁸

7. PNM also proposes to discontinue providing energy imbalance and spinning and supplemental reserve services to Navopache.⁹ Navopache estimates that the costs to acquire these services will be approximately \$1.02 million.¹⁰ Finally, PNM proposes a number of miscellaneous deletions and additions in the Amended Agreement that vary from the 1999 Agreement.

III. Notice of Filing and Responsive Pleadings

8. Notice of PNM's filing was published in the *Federal Register*, 76 Fed. Reg. 59,675 (2011) with interventions and protests due on or before October 6, 2011.¹¹ Navopache filed a timely protest. On October 28, 2011, PNM filed a motion for leave to answer and answer.

IV. Discussion

A. Procedural Issues

9. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2011), the notice of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2011), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We are not persuaded to accept PNM's answer, and will, therefore, reject it.

⁸ *Id.*

⁹ Amended and Restated Power Sale Agreement at 19.

¹⁰ Navopache Protest at 11, n.45.

¹¹ The Commission subsequently extended the date for interventions and protests to October 14, 2011.

B. Navopache's Protest

10. In its protest, Navopache argues that PNM failed to follow the Commission's clear requirement to use the median ROE from the proxy group selected. Further, Navopache challenges PNM's exclusion of PNM from the proxy group. Navopache argues that a company excluding itself from a proxy group is inconsistent with Commission policy, and contends that PNM does not offer explanation or justification for deviating from this policy. Navopache also contends that PNM miscalculated the median value ROE.¹² In addition, Navopache argues that PNM requests an unauthorized 124 basis point ROE adder to offset the performance of non-regulated businesses, and that PNM does not justify this proposed risk premium. Navopache contends that PNM does not have unique risks that would warrant such an increase. Moreover, Navopache argues that PNM proposes to add accumulated deferred income tax, pre-paid pension costs, cash working capital, production plant property tax, and acquisition adjustment premiums for Palo Verde Nuclear Generating Station Units 1 and 2 to its rate base without support.¹³

11. Navopache claims that PNM has changed the costs for transmission across the APS system from transmission to merchant costs, which PNM argues makes such costs directly assignable to Navopache. Navopache asserts that such direct assignment is not part of the parties' 1999 Agreement and is not supported by the course of the parties' performance under such agreement.¹⁴

12. Navopache argues that PNM proposes to cease providing ancillary services to Navopache, and that such action is not permitted by the 1999 Agreement.¹⁵ Finally, Navopache states that PNM unilaterally proposes six pages of changes to the 1999 Agreement that have nothing to do with rates and as such, are also not permitted by the 1999 Agreement.¹⁶ Navopache also argues that PNM has not negotiated in good faith,

¹² Navopache Protest at 24-26.

¹³ *Id.* at 29-32. PNM includes an acquisition adjustment of \$4,488,567 in its rate base and an amortization expense adder for the acquisition adjustment of \$365,100. PNM Ex. No. Period II, Statement BK, at 8 and 15.

¹⁴ Navopache Protest at 7, 14-17.

¹⁵ *Id.* at 10.

¹⁶ *Id.* at 11-12.

that PNM has no authority to propose these changes, and that under the *Mobile-Sierra*¹⁷ doctrine the Commission may not accept any of these changes absent a finding that they are required by the public interest.

V. Commission Determinations

13. PNM's proposal raises issues that cannot be resolved based on the record before us, and are more appropriately addressed in the hearing and settlement judge procedures ordered below, including whether the changes are permitted to be filed under the parties' agreement (as Navopache observes), and if so, whether they are subject to the ordinary just and reasonable standard of review, or to the more stringent version of that standard known as the public interest standard. The Commission will, however, decide the median/midpoint issue here, since it has previously determined that with regard to a single utility's proposed base ROE, the use of the median—not midpoint—discounted cash flow value from the proxy group selected is the most accurate measure of central tendency for a single utility of average risk, such as PNM.¹⁸ Therefore, we direct PNM to use the median to establish the base ROE.¹⁹

14. Our preliminary analysis indicates that PNM's proposed rates have not been shown to be just and reasonable and may be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful. In *West Texas*,²⁰ the Commission explained that when our preliminary analysis indicates that the proposed rates may be unjust and unreasonable, and may be substantially excessive, as defined in *West Texas*, the Commission will generally impose a five-month suspension. In the instant proceeding, we find that the proposed rates may be substantially excessive. Therefore, we will accept PNM's proposed rates for filing, suspend them for five months, subject to refund, and set them for hearing and settlement judge procedures.

15. In addition, the Commission's policy on acquisition adjustments in cost-based rates is to allow them only when an applicant can demonstrate that the acquisition

¹⁷ *United Gas Pipe Line v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) and *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Mobile-Sierra*).

¹⁸ *Southern California Edison Co.*, 136 FERC ¶ 61,074, at P 30 (2011)

¹⁹ In this order, we only direct the use of the median in calculating the ROE; we are not thereby adopting PNM's calculation of the median at 9.48 percent. Thus, the appropriate calculation of the median remains to be determined at hearing.

²⁰ *West Texas Utilities Co.*, 18 FERC ¶ 61,189 (1982) (*West Texas*).

provides specific, measurable, and substantial benefits to ratepayers.²¹ At the hearing, PNM must submit evidence demonstrating that its acquisition adjustments satisfy the Commission's policy requirements.

16. While we are setting these matters for a trial-type evidentiary hearing, we encourage the parties to make every effort to settle their disputes before hearing procedures are commenced. To aid the parties in their settlement efforts, we will hold the hearing in abeyance and direct that a settlement judge be appointed, pursuant to Rule 603 of the Commission's Rules of Practice and Procedure.²² If the parties desire, they may, by mutual agreement, request a specific judge as the settlement judge in the proceeding; otherwise, the Chief Judge will select a judge for this purpose.²³

17. The settlement judge shall report to the Chief Judge and the Commission within 30 days of the date of this order concerning the status of settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions or provide for commencement of a hearing by assigning the case to a presiding judge.

The Commission orders:

(A) PNM's filing is hereby accepted for filing and suspended for five months, to be effective April 14, 2012, subject to refund and hearing as discussed in the body of this order and the ordering paragraphs below.

(B) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Commission by section 402(a) of the Department of Energy Organization Act and by the FPA, particularly sections 205 and 206 thereof, and pursuant

²¹ *Promoting Transmission Investment through Pricing Reform*, Order No. 679, FERC Stats. & Regs. ¶ 31,222, at P 258 (2006), *order on reh'g*, Order No. 679-A, FERC Stats. & Regs. ¶ 31,236, *order on reh'g*, 119 FERC ¶ 61,062 (2007). *See also Longhorn Partners Pipeline*, 82 FERC ¶ 61,146 (1998); *Minnesota Power & Light Co.*, 43 FERC ¶ 61,104, at 61,342, *reh'g denied*, 43 FERC ¶ 61,502 (1988); *Duquesne Light Holdings Inc.*, 117 FERC ¶ 61,326, at n.47 (2006); *Montana-Dakota Utilities Co.*, 23 FERC ¶ 61,151 (1983); *Longhorn Partners Pipeline*, 73 FERC ¶ 61,355 (1995).

²² 18 C.F.R. § 385.603 (2011).

²³ If the parties decide to request a specific judge, they must make their joint request to the Chief Judge by telephone at (202) 502-8500 within five days of this order. The Commission's website contains a list of Commission judges and a summary of their background and experience (www.ferc.gov – click on Office of Administrative Law Judges).

to the Commission's Rules of Practice and Procedure and the regulations under the FPA (18 C.F.R. Chapter I), a public hearing shall be held concerning the justness and reasonableness of the proposed revisions. However, the hearing shall be held in abeyance to provide time for settlement judge procedures, as discussed in Ordering Paragraphs (C) – (E) below.

(C) Pursuant to Rule 603 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.603 (2011), the Chief Administrative Law Judge is hereby directed to appoint a settlement judge in this proceeding within fifteen (15) days of the date of this order. Such settlement judge shall have all the powers and duties enumerated in Rule 603 and shall convene a settlement conference as soon as practicable after the Chief Judge designates the settlement judge. If the parties decide to request a specific judge, they must make their request to the Chief Judge in writing or by telephone within five days of the date of this order.

(D) Within 30 days of the date of this order, the settlement judge shall file a report with the Commission and the Chief Judge on the status of the settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions, if appropriate, or assign this case to a presiding judge for a trial-type evidentiary hearing, if appropriate. If settlement discussions continue, the settlement judge shall file a report at least every 60 days thereafter, informing the Commission and the Chief Judge of the parties' progress toward settlement.

(E) If settlement judge procedures fail and a trial-type evidentiary hearing is to be held, a presiding judge, to be designated by the Chief Judge, shall, within 15 days of the date of the presiding judge's designation, convene a prehearing conference in this proceeding in a hearing room of the Commission, 888 First Street, NE, Washington, DC 20426. Such a conference shall be held for the purpose of establishing a procedural schedule. The presiding judge is authorized to establish procedural dates and to rule on all motions (except motions to dismiss) as provided in the Commission's Rules of Practice and Procedure.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.