

111 FERC ¶ 61,305
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeen G. Kelly.

American Electric Power Service Corporation

Docket No. ER05-751-000

ORDER ACCEPTING AND SUSPENDING PROPOSED TARIFF REVISIONS,
SUBJECT TO REFUND,
AND ESTABLISHING HEARING PROCEDURES

(Issued May 31, 2005)

1. As discussed below, we accept American Electric Power Service Corporation's (AEP) proposed increased transmission rate, as modified below, suspend the proposed rate for five months, to become effective November 1, 2005, subject to refund, and establish hearing procedures.
2. This order benefits customers by providing AEP timely recovery of just and reasonable transmission rates for service over AEP's transmission facilities.

I. Background

3. AEP offers open access transmission service over its facilities pursuant to its open access transmission tariff (OATT). The transmission and ancillary service rates for AEP's east zone were established in Docket No. ER98-2786-000.¹ In *Opinion No. 442*, the Commission approved the merger of AEP and Central South West Corporation (CSW) on the condition, among others, that AEP and CSW join a Commission-approved regional transmission organization (RTO) and transfer operational control of its transmission facilities to the RTO. On September 28, 2004, among other things, the Commission accepted AEP's transmission rates to become effective on the date that its

¹ See *American Electric Power Company*, 85 FERC ¶ 61,201 (1998), *Opinion No. 442*, 90 FERC ¶ 61,242 (2000), *order on reh'g*, 91 FERC ¶ 61,129 (2000), *Opinion No. 442-A, appeal denied sub nom. Wabash Power Association v. FERC*, 268 F.3d 1105 (D.C. Cir. 2001) (*Opinion No. 442*).

transmission facilities were integrated into PJM Interconnection, L.L.C. (PJM)² and directed AEP to file revised rates to become effective January 1, 2005.³ On October 28, 2004, PJM submitted AEP's revised zonal rates.⁴

4. On November 17, 2003, concurrent with the CSW merger proceedings and the integration of AEP into PJM, the Commission ordered the elimination of regional through and out (T&O) rates between PJM and Midwest Independent Transmission System Operator, Inc. (Midwest ISO) effective April 1, 2004, and authorized a transitional Seams Elimination Charge/Cost Adjustments/Assignments (SECA) to be effective, subject to refund, through March 31, 2006.⁵ On November 18, 2004, the Commission rejected AEP's et al., Regional Pricing Plan, intended to supersede the SECA after March 31, 2006, and ordered a SECA compliance filing.⁶ On November 24, 2004, PJM and Midwest ISO and PJM Transmission Owners (including AEP) submitted the SECA compliance filings required by the November 18 Order. On November 30, 2004, the Commission issued an order clarifying that AEP's SECA compliance filing may include lost revenues associated with PJM intra-RTO rate pancaking as well as the elimination of inter-RTO regional T&O rates between PJM and Midwest ISO utilizing the SECA transition methodology. On February 10, 2005, the Commission accepted the SECA compliance filings to take effect December 1, 2004, subject to refund and surcharge as appropriate, and set them for hearing.⁷

²See *PJM Interconnection, L.L.C.*, 108 FERC ¶ 61,318 (2004), *reh'g denied*, 110 FERC ¶ 61,395 (2005) (*PJM I*). AEP integrated its operating companies into PJM on October 1, 2004.

³The Commission accepted AEP's commitment to update its network service rates to reflect a 1-CP (coincident peak) rate divisor based on actual 2004 loads. *Id.*, 108 FERC ¶ 61,318 at P 27-28.

⁴The proposed revised zonal rates are pending before the Commission. *See generally, PJM I* (Commission ordered compliance filing and accepted tariff sheets subject to outcome of the regional through and out rate proceedings in Docket Nos. EL02-111-000 and EL03-212-000).

⁵See, *Midwest Independent Transmission System Operator, Inc.*, 104 FERC ¶ 61,105, *order on reh'g*, 105 FERC ¶ 61,212 at P 42 (2003) (November 17 Order), *reh'g pending*.

⁶See *Midwest Independent Transmission System Operator, Inc.*, 109 FERC ¶ 61,168 (2004).

⁷See *Midwest Independent Transmission System Operator, Inc., et al.*, 110 FERC ¶ 61,107 (2005) (*Midwest ISO*).

II. Rate Filing

5. In the instant filing, AEP, on behalf of Appalachian Power Company, Columbus Southern Power Company, Indiana Michigan Power Company, Kentucky Power Company, Kingsport Power Company, Ohio Power Company and Wheeling Power Company (collectively, AEP Companies) filed a proposed two-step increase for AEP's east zonal transmission rates to be included in the PJM OATT.⁸ The proposed changes include a transmission cost of service (TCOS), a SECA credit, and a production cost of service (PCOS) designed to develop the cost-based revenue requirements and rates for both transmission and ancillary services for AEP's East Zone companies. AEP proposes a historic Period I of twelve months ending December 31, 2003, and a projected Period II test period of twelve months ending December 31, 2005. AEP states that the proposed annual TCOS, net of grandfathered transmission contracts and other operating revenues allocated to the transmission function, is \$486.1 million.

6. The proposed rates would result in an increase of \$42.7 million for Network Transmission service, a decrease for Point-to-Point service, and an increase of \$13.6 million in the PCOS for AEP's Reactive Supply and Voltage Control services. AEP seeks a rate of return on equity (ROE) of 12 percent plus a 50 basis points upward adjustment of the ROE consistent with *Midwest ISO*. AEP states that, based on its experience in the T&O rate elimination proceeding (Docket Nos. EL02-111-000 and EL03-212-000), it expects several parties to protest the level and existence of its SECA. AEP also states that an initial decision on the proposed SECA rates is not expected until after the SECA is eliminated in April 2006. Accordingly, as the second step rate increase, AEP proposes to increase its TCOS rates by an additional 51 percent in April 2006 to reflect expiration of the SECA credits. AEP has also included a true-up provision in the PJM OATT for Network and Point-to-Point transmission rates to reflect the outcome of the SECA proceeding. AEP requests an effective date for its proposed rates of June 1, 2005.

III. Notice Of Filing, Interventions And Protests

7. Notice of the filing was published in the *Federal Register*, 70 Fed. Reg. 19,752 (2005), with protests and interventions due on or before April 21, 2005. Motions to intervene or motions for late intervention were filed by the entities listed in Attachment A to this order.⁹ On May 16, 2005, AEP filed an answer to motions to intervene and

⁸ AEP proposes Attachment H-14, and *pro forma* Schedules 1A, 2, 7, 8 and Attachment H-A to the PJM OATT. AEP's west zone transmission facilities are not located in PJM's footprint therefore rates for those facilities are not at issue here.

⁹ The comments and protests will be discussed below.

protest. On May 19, 2005, Detroit Edison Company, Consumer Energy Company, CMS Energy Resource Management Company filed a joint answer to AEP's answer.

8. A number of parties oppose AEP's two-stepped increases as excessive and therefore not just and reasonable. They argue that after the SECA credit is eliminated, the second step rate increase will produce a substantial and unreasonable cost shift to those entities that serve load in the AEP east zone. Protestors also argue that removing the SECA revenue credit offset after Period II is prohibited by the Commission's policy against *ad hoc* and piecemeal adjustments.¹⁰ They assert that AEP's rate base will decline through depreciation and load will grow in 2006 and if the proposed rates are in effect at that time the rates will become excessive, unjust and unreasonable. Accordingly, protestors request that the Commission reject the proposed post-test-year, "piecemeal adjustment" to remove all SECA revenues.¹¹

9. The protestors also object to the proposed 12 percent ROE as excessive and the 50 basis point adder is unjustified because they assert that AEP should not be rewarded for joining an RTO and because it will increase consumer costs, decrease public support, undermine state-federal comity, and may have the opposite effect than that sought by the Commission. Many protestors also object to AEP's application of the Discounted Cash Flow (DCF) model in the determination of the ROE. They also allege errors in AEP's proxy applications, unwarranted leverage adjustments, ballooned flotation cost adjustments, and improper use of a midpoint of extremes rather than the median of all calculated ROEs. The VIM Customers argue that the proxy group selection criteria used by AEP's witness, Dennis W. Bethel, does not identify the risk and cost of capital invested in the AEP-owned facilities used to provide the rate-regulated services at issue.¹²

10. Protestors assert that AEP overstated its rate base in several ways. For example, Wabash Valley and VIM Customers assert that aggregation of AEP's cost of service information reveals that AEP has included, without support, approximately \$133 million of transmission plant additions from the beginning to the end of the 2005 estimated test year and a total of approximately \$209 million from December 31, 2003. Consumers

¹⁰ Citing *Delmarva Power & Light Company*, 38 FERC ¶ 61,098 at 61,259 (1987), *reh'g denied*, 43 FERC ¶ 61,520, *aff'd mem.*, No. 88-1557 (D.C. Cir. 1989); *Southwestern Public Service Co.*, 63 FERC ¶ 61,295 at 63,093 n.12 (1993); *Carolina Power & Light Company v. FERC*, 860 F.2d 1097 (D.C. Cir. 1988).

¹¹ See VIM protest at p. 4-6 and Wabash Valley protest at 17-18.

¹² Citing *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944), *Bluefield Water Works & Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923); *accord Southern California Edison Co.*, 92 FERC ¶ 61,070, 61,263-64 (2000), *order on remand*, 107 FERC ¶ 61,115, *reh'g denied*, 108 FERC ¶ 61,085 (2004).

Energy and Ormet contend that AEP's transmission plant includes low voltage facilities that do not provide a transmission function because AEP has failed to properly utilize a Seven Factor Test to classify its transmission facilities.¹³ Many protestors also note that the filing is deficient because AEP did not provide studies for allocations of general and intangible plant, pension funding, and property taxes.

11. Protestors raise numerous other issues regarding AEP's TCOS. For example, they argue that the proposed \$2 million of RTO start-up costs is unsupported. According to VIM Customers, it is unreasonable to retain the existing 3.3 percent losses when the prevailing losses in PJM are 3 percent on peak and 2.5 percent off peak. Protestors also object to the proposed rates because AEP provides \$1.7 million in transmission related revenue credits but AEP shows almost \$100 million in Account 454, Rent from Electric Property. Additionally, protestors complain that AEP has improperly allocated advertising and state regulatory commission expenses to transmission. Ormet asserts that AEP should offer voltage-differentiated rates. AMP-Ohio argues that AEP should not have made individual cost of service filings for each of its seven operating companies without providing workpapers in the format that can be more easily analyzed. Wisconsin Electric seeks assurance that AEP's cost of service increase will not affect PJM's T&O rate for existing transactions.

12. The protestors also object to AEP's PCOS, asserting that the proposed rates for reactive power and VAR production are unsupported. They note that many of their proposed adjustments to AEP's TCOS also apply to the production plant used to supply reactive power. Protestors also contend that AEP: (1) double counted its generation step-up transformers; (2) failed to include accumulated deferred income taxes for all the AEP Companies; (3) improperly allocated operations and maintenance expenses; and (4) improperly increased the allocation factors by rounding. Protestors request that the Commission find the filing deficient, or in the alternative, set the filing for full

¹³ The Commission developed a seven factor test to determine what facilities are transmission facilities and what facilities are local distribution facilities to determine which facilities would be under Commission jurisdiction and which facilities would remain subject to state jurisdiction for retail regulatory purposes. *See Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, 61 Fed. Reg. 21,540 (1996), FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996 ¶ 31,036 at 31,783-84 (1996), *order on reh'g*, Order No. 888-A, 62 Fed. Reg. 12,274 (1997), FERC Statutes and Regulations ¶ 31,048 (1997), *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom. New York v. FERC*, 535 U.S. 1 (2002).

evidentiary hearing. The protestors also request a five-month suspension of the proposed transmission rates.¹⁴

IV. Discussion

A. Procedural Matters

13. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2004), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. Given the early stage of this proceeding, the absence of any undue prejudice or delay, and the parties' interest in this proceeding, we will grant the untimely motions to intervene. Rule 213(a) (2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. §385.213(a) (2) (2004), prohibits an answer to an answer unless otherwise ordered by the decisional authority. We are not persuaded to accept AEP's answer and will, therefore, reject it. Nor will we accept the joint answer to AEP's answer filed by some of the protestors.

B. Analysis

1. ROE Adder

14. Protestors complain that the 50 basis point ROE adder is unjustified because AEP should not be rewarded for being required to join an RTO as a condition of its merger. They argue that AEP acquired CSW in order improve the return to its stockholders and AEP should not also be rewarded for complying with a condition of that merger. The Commission finds that the issue of whether it is appropriate in these circumstances to allow a 50 basis point adder to the ROE is one that should be included in the hearing we are ordering herein to ensure the development of a full record on which we can base our decision.

2. SECA Revenues

15. Protestors request that the Commission reject the proposed post-test-year, "piecemeal adjustment" to remove all SECA revenues. Although we agree with the protestors that the Commission has a general policy against reflecting post-test period data in the test year¹⁵, we have allowed exceptions to our general policy when the post-

¹⁴ *Citing West Texas Utility Company*, 18 FERC ¶ 61,189 (1982) (*West Texas*).

¹⁵ *See, e.g., Williston Basin Interstate Pipeline Company*, 87 FERC ¶ 61,265 at 61,021 n.33 (1999) (*Williston*); *Public Service Company of Indiana*, 7 FERC ¶ 61,319 at 61,702, *reh'g denied*, 8 FERC ¶ 61,224 (1979); *Union Electric*, 47 FPC 144, 150 (1972).

test period data show that projections based on test period data will be seriously in error.¹⁶ In this case, AEP claims that the elimination of the SECA credit will necessitate an approximate 51 percent increase in its proposed transmission rates beginning in April 2006. Also, the April 1, 2006 changes do not reflect the use of out of test period costs, but instead reflect a change in rate design mandated by the Commission. In light of these considerations, we will accept the post April 1, 2006 rates, subject to refund, and set these rates for consideration at the hearing.

16. We also note that the final outcome of the pending proceeding concerning the long-term pricing structure (LTPS) for transmission between PJM and Midwest ISO is uncertain and could affect the rates proposed by AEP in this proceeding. Specifically, it is uncertain whether there will be a mechanism in place to recover through and out costs after the SECA expires, and if so the extent to which such mechanism would allow AEP to recover such costs. Because the final outcome of these matters may reduce or eliminate the need for the proposed second step rate increase, any rates approved by the Commission in this proceeding will be subject to the outcome of the proceedings in Docket No. EL02-111-000.¹⁷

3. Hearing Procedures

17. AEP's proposed rate increase raises issues of material fact that cannot be resolved based on the record before us, and are more appropriately addressed in the hearing ordered below. We agree with protestors that AEP has failed to provide adequate support for a number of its proposed changes and therefore we direct the presiding administrative law judge to permit the parties appropriate discovery of these matters.

18. Our preliminary analysis indicates that the proposed rate has not been shown to be just and reasonable, and may be unjust, unreasonable, unduly discriminatory or preferential or otherwise unlawful. Accordingly, we will accept the proposed rate for filing, as modified herein, suspend it, and set it for hearing.

19. In *West Texas* 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 would generally impose a five month suspension. In the instant proceeding, our preliminary analysis

¹⁶ See, e.g., *Williston*, 87 FERC at 62,022; *DistriGas of Mass. Corp. v. FERC*, 737 F.2d at 1220; *National Fuel Gas Supply Corp.*, 51 FERC ¶ 61,122 at 61,334 (1990), *reh'g denied*, 55 FERC ¶ 61,269 (1991).

¹⁷ This condition will protect customers in the unlikely event that customers will fail to insist on changes to AEP's post March 31, 2006 rates in the SECA section 206 proceedings.

indicates that the proposed rate may be substantially excessive. Therefore, we will accept AEP's proposed rate, as modified above, suspend it for five months to be effective November 1, 2005, subject to refund, and set the matter for hearing.

The Commission orders:

(A) AEP's proposed rate is hereby accepted for filing, suspended for five months to become effective November 1, 2005, subject to refund.

(B) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by section 402(a) of the Department of Energy Organization Act and by the Federal Power Act, particularly sections 205 and 206 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the Federal Power Act (18 C.F.R., Chapter I), a public hearing shall be held in Docket No. ER05-751-000 concerning the justness and reasonableness of the proposed rate, as revised herein, and as discussed in the body of this order.

(C) A presiding administrative law judge, to be designated by the Chief Administrative Law Judge, shall convene a prehearing conference in these proceedings, to be held within approximately fifteen (15) days from the date of this order, in a hearing room of the Federal Energy Regulatory Commission, 888 First Street, NE, Washington, D.C. 20426. Such 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)

Linda Mitry,
Deputy Secretary.

Interventions

Allegheny Power
Appalachian Power Company, et al (AEP Companies)
Blue Ridge Power Agency and Old Dominion Electric Cooperative
Calpine Corporation
Cities of Dowagiac and Sturgis, Michigan
CMS Energy Resource Management Company*
Duke Energy Marketing America, LLC
Duke Energy Trading and Marketing LLC
Exelon Corporation
FirstEnergy Service Company
Indiana and Michigan Distributors Association and its Members
Indiana Municipal Power Agency
ISO New England Inc.
Michigan Public Service Commission
Mittal Steel USA ISG Inc.
North Carolina Electric Membership Corporation
Ohio Energy Group
Old Dominion Electric Cooperative
PJM Interconnection
Public Utilities Commission of Ohio
Southeastern Power Administration
The Public Service Commission of the Commonwealth of Kentucky
US Dept of Energy – Southeastern Power Administration
Virginia Electric and Power (Dominion VA)
Virginia State Corporation Commission

Comments and Protests

AEP Intevenor Group
American Municipal Power – Ohio, Inc. (Amp-Ohio)
Blue Ridge Power Agency
Buckeye Power Inc.
Consumers Energy Company (Consumers Energy)
The Detroit Edison Company
Ormet Primary Aluminum Corporation (Ormet)
Steel Dynamics, Inc.
Virginia, Indiana and Michigan Transmission Customers (VIM Customers)
Wabash Valley Power Association, Inc. (Wabash Valley)
Wisconsin Electric Power Company (Wisconsin Electric)

* Intervention was out of time.