UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Northeast Utilities Service Company   Docket No. ER06-275-000

ORDER ACCEPTING TARIFF REVISIONS

(Issued January 31, 2006)

1. In this order, we accept Northeast Utilities Service Company's (NUSCO) December 1, 2005 filing, on behalf of its affiliated operating companies, The Connecticut Light and Power Company, Western Massachusetts Electric Company, Holyoke Power and Electric Company, Holyoke Water Power Company, and Public Service Company of New Hampshire (collectively, NU). The filing revises Schedule 21-NU of section II of ISO New England Inc.'s (ISO-NE) Transmission, Markets and Services Tariff, which is the ISO-NE Open Access Transmission Tariff (ISO-NE OATT). NU proposes to modify its transmission rates for Local Network Service (LNS) under Schedule 21-NU to include in rate base fifty percent of construction work in progress (CWIP) related to four major transmission projects that NU will build over the next several years in Southwest Connecticut. NU requests an effective date of February 1, 2006, which we will grant.

Background

2. The NU Companies are public utility subsidiaries of Northeast Utilities, a registered public utility holding company. The NU Companies own and operate transmission facilities in the states of Connecticut, Massachusetts and New Hampshire. Their facilities are used to provide Regional Network Service (RNS) under the ISO-NE OATT and Local Network Service under Schedule 21-NU of the ISO-NE OATT. The NU Companies are Participating Transmission Owners (PTOs) in the New England RTO.

3. Transmission rates under Schedule 21-NU are calculated based on projected costs that are later trued up to reflect actual costs. Under its existing procedures, NU accrues

an allowance for funds used during construction (AFUDC)[1] on its books while transmission projects are under construction but does not include the cost of new transmission projects in rate base until the project is placed in service. NU proposes to modify its LNS rate to provide for the inclusion of fifty percent of CWIP in rate base for four specific projects in accordance with Section 35.25 of the Commission's regulations, 18 C.F.R. § 35.25. NU states that this proposed modification will allow NU to recover its costs during construction and improve its cash flow during a time when it will be required to finance a significant expansion of its transmission system. NU states further that while the inclusion of CWIP in rate base will increase transmission rates during the construction period, CWIP in rate base results in a lower future rate base than would occur by accruing AFUDC.[2]

4. NU states that the transmission system in Southwest Connecticut (SWCT) is one of the most congested in the country and faces grave reliability concerns because of transmission deficiencies. NU states that the Commission has recognized SWCT as an area facing significant reliability concerns and in need of reinforcement.[3] NU states further that each of the four projects is included in ISO-NE's Regional System Plan (RSP) for 2005[4] and each has been granted siting approval by the State of Connecticut. NU states that ISO-NE, the Connecticut Department of Public Utility Control, and the Connecticut Siting Council have recognized the weakness of SWCT's transmission system and its failure to meet national and regional reliability standards. According to

[1] A regulated utility is entitled to recover its costs plus a reasonable return on its investment. One of its costs is the amount it spends to finance construction of new facilities. This cost includes debt interest and a reasonable return on equity on the capital investment used to finance the construction. There are two ratemaking methodologies by which these carrying charges on construction capital are recovered in the utility's rates. One method is to capitalize the carrying charges incurred during construction as AFUDC. Under this method, ratepayers do not make payments until after the plant goes into service.

[2] NU also proposes a change to Schedule 21-NU to include CWIP and AFUDC as items subject to a requirement that the NU Companies make rate base adjustments to estimates, and in the true-up process, reflect the in-service dates for capital additions where costs exceed $20 million.

[3] *Devon Power LLC*, 107 FERC ¶ 61,240 at PP 43, 49 (2004).

[4] The ISO-NE's Regional System Plan is a planning report that identifies system improvements needed over the next 10 years.

NU's analysis, the system deficiencies in SWCT can be attributed to several factors, including (1) an inadequate transmission system because it is not served by the interregional 345-kV transmission grid; (2) restrictions on the development of new generating plants resulting from transmission constraints; (3) an increased peak customer demand for electricity that exceeds existing transmission service capabilities; and (4) existing generation and transmission system interdependencies that restrict the full dispatch of generation resources to service customer demand for electricity.

5. NU, through CL&P, has undertaken the construction of four major transmission projects in the SWCT area. The four projects are described in detail in the testimony accompanying NU's application and are summarized below.

6. The Bethel-Norwalk Project is the first phase of a proposal to extend the 345-kV transmission system into the SWCT load pocket. The Project is now under construction and consists of a new 20.4-mile, 345-kV transmission circuit between Plumtree Station in Bethel and Norwalk Substation in Norwalk, including 11.8 miles of 345-kV underground cables. NU estimates that the total cost of the Bethel-Norwalk Project will be $350 million, and expects that the Project will be placed in service during the fourth quarter of 2006. NU states that significant expenses were incurred in 2005, and will continue into December 2006 when the project is scheduled to be completed.

7. The second project is the Middletown-Norwalk Project which extends approximately 70 miles from CL&P's existing substations in Middletown to the new 345-kV Substation being constructed at Norwalk as part of the Bethel to Norwalk Project. NU states that the Middletown-Norwalk Project will complete the new 345-kV loop into SWCT by providing a second transmission link into the City of Norwalk from central Connecticut and from points in Milford and Bridgeport. NU states that the total cost of the Middletown-Norwalk Project is estimated to be approximately $1,047 million and is scheduled to be in service in the fourth quarter of 2009. According to NU, the greatest expense will be incurred in 2007, continuing through 2008, when part of the project will begin service, and into 2009 when the project is completed.

8. The third project is the Glenbrook Cables Project, to be constructed by CP&L. The project consists of two new 115-kV underground transmission lines from the Norwalk Substation to the Glenbrook Substation in Stamford. NU states that the project is needed to provide a reliable electric supply in southwest Fairfield County. NU estimates that this project will cost an estimated $120 million and is expected to be in service in the fourth quarter of 2008. NU states that the heaviest expenses will occur in 2008.

9. The fourth project is the Long Island Replacement Project (LIRC Project). An existing submarine electric transmission cable system extending from CL&P's Norwalk

Harbor Substation to the Long Island Power Authority's (LIPA) will be removed and replaced. The cost of the project will be shared equally between CL&P and LIPA, but CL&P will manage the project on behalf of itself and LIPA. The estimated cost for CL&P's share of the project is approximately $72 million with the heaviest expenses occurring in 2007. The project is expected to be in service in the second quarter of 2007.

10. NU states that the need for the Bethel-Norwalk, Middletown-Norwalk, Glenbrook Cables, and the LIRC Projects is supported by findings of both the ISO-NE and the CSC. NU submits that all of the projects have been reviewed during extensive hearings before the CSC, which included consideration of various alternatives to each of the projects. NU submits further that the CSC's review process took into account a number of other factors, such as route alternatives, electric and magnetic field issues, and engineering costs. NU has included with its application a summary of the ISO-NE's Regional Plan for 2005, together with excerpts of applications to the CSC for project approval, and the CSC's Findings of Fact with regard to each project. NU submits that the projects are needed to satisfy National Electricity Reliability Council and Northeast Power Coordinating Council reliability standards and to provide greater access to competitively priced generation.

11. NU estimates that the total cost of construction for the four projects will exceed $1.5 billion. NU states that it is in the middle of the construction process and is expending large amounts of capital to build the projects. NU states that its transmission rate base is expected to grow significantly over the next few years, from approximately $46 million at the end of 2004 to nearly $2.4 billion by the end of 2010. NU has provided numerous exhibits demonstrating that NU has chosen the least-cost construction alternatives, including the use of existing right of ways whenever possible, minimization of congestion costs while constructing transmission line facilities, and allowing the building of needed facilities without undue risk of interrupting customer service.[5]

12. NU states that its proposed modifications to Schedule 21-NU, to include 50 percent of CWIP in rate base, is limited to the four transmission projects discussed above. NU states that if it seeks CWIP treatment for any additional transmission projects, it will make a new filing with the Commission. NU states that it will implement accounting procedures to ensure that transmission customers will not be charged for both AFUDC

[5] See NU's Exhibit NU-15 at p G-1. See also NU Exhibit NU-13 at H-4; Exhibit NU-14 at p 78, and Exhibit NU-16 at p 292.

and corresponding amounts of CWIP.[6] NU states that it will submit an annual report to the Commission containing information as to the amounts of CWIP recorded for each of the SWCT projects, related accounts, such as AFUDC and regulatory liability, and the resulting effect on the CWIP revenue requirements.

Notice of Filings and Responsive Pleadings

13. Notice of NU's filing was published in the *Federal Register*, 70 Fed. Reg. 76,278 (2005), with protests or interventions due on or before December 22, 2005. On December 22, 2005, New Hampshire Electric Cooperative, Inc. and United Illuminating filed motions to intervene. On the same date, Unitil Energy Systems, Inc. (Unitil) filed a motion to intervene and comments. On January 6, 2006, NU filed an answer to Unitil's comments, and on January 23, 2006, Unitil filed reply comments to NU's answer, requesting that the Commission accept NU's answer and Unitil's reply comments since they outline further commitment to address a potential reallocation of costs.

14. Unitil does not oppose NU's proposal to include 50 percent of the CWIP for the SWCT Projects in NU's rate base. Rather, Unitil is concerned with cost allocation and whether the costs are properly allocated in accordance with the provisions of Schedule 21-NU. Unitil states that NU's costs for local service, *i.e.*, costs that recover the portions of NU's transmission requirement not recovered elsewhere, are calculated within two formula rates (Category A and Category B) from two different groups of customers. Category A rates includes the NU Companies' total transmission costs. Category A costs are recovered from all customers receiving LNS service under NU's tariff. Category B costs are any Pool Transmission Facilities (PTF) costs excluded from the regional revenue requirement on the grounds that such costs are localized costs and should be recovered only from customers located in the area where the expenditures are made. Revenues recovered under the Category B rates are subtracted from the revenue requirement used to determine Category A rates. Unitil states that at this stage of the proceeding, it lacks sufficient information to determine whether any of the costs of the proposed projects should be recovered as Category B costs. Unitil requests that the Commission direct NU to provide additional information indicating the appropriate cost allocation and that the Commission review the proposed cost allocation. Unitil states that if costs are found that should be classified as Category B costs, the Commission should

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[6] While the projects are being constructed, NU will accrue AFUDC on 100 percent of the CWIP balance. However, to reflect the fact that fifty percent of CWIP will be included in rate base for Schedule 21-NU customers, a regulatory liability will be recorded to offset fifty percent of the recorded AFUDC.

direct NU to recover the CWIP associated with such costs from local customers in Connecticut. Unitil states that at a minimum, a mechanism should be in place to track the recovery of the costs so that when a determination regarding localized costs is finally made, appropriate reallocations can be made.

15. On January 6, 2006, NU filed an Answer in response to Unitil's comments. NU states that Unitil's comments are premature since ISO-NE has not yet made a determination on the localization of costs associated with any of the projects, pointing out that such determination is required by Schedule 12 C of the ISO-NE OATT[7]. NU states further that, pursuant to the Commission's order approving NU's formula rates, it has an obligation to make a localized cost filing after a final determination that any costs associated with the SWCT Projects should be localized.[8] NU states that before it charges any customers for Category B costs, it will make a filing with the Commission and provide a mechanism to ensure that no customer is responsible for any costs that are localized to another jurisdiction. If adjustments are necessary, NU states that it will propose a true-up mechanism to calculate any amounts that may have been overpaid, and make refunds to those customers. NU states that Unitil and other parties will have the opportunity to raise any concerns at the time it makes its localized cost filing.

Discussion

Procedural Matters

16. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2005), the timely, unopposed motions to intervene are granted. Rule 213(a) (2) of the Commission's Rules of Practice and Procedure prohibits the filing of answers to protests unless otherwise permitted by the decisional authority. We find good cause in this proceeding to allow NU Companies' answer and Unitil's response to NU's answer because they provide information that aids us in our understanding and resolution of the issues.

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[7] NU states that the determination of cost allocation for the Bethel-Norwalk Project will not be made by ISO-NE until later in the first quarter of 2006, and localized cost determinations on the other three projects are not expected to be available until sometime in 2007.

[8] *Northeast Utilities Service Co.*, 105 FERC 61,089 at PP 3, 25 (2003).

Commission Discussion

17. In Order No. 298[9], as further explained in *Boston Edison*[10], we permitted utilities to file to include CWIP in rate base. Instead of accruing AFUDC, utilities may, under certain conditions, include CWIP in rate base and thereby recover carrying charges on a current basis. To prevent double recovery of carrying costs, AFUDC is not capitalized on the CWIP included in rate base.

18. In Order No. 298, and in *Boston Edison*, we stated that the CWIP issue is mainly a timing issue. If the company utilizes the AFUDC approach, the utilities' future revenues and customers' future rates are higher than they would be if CWIP had been used.[11] We recognized that allowing CWIP improves utilities' cash-flow in a less costly manner than if AFUDC is added to the cost of construction since CWIP in rate base results in a lower future rate base and lower future rates. We also found that the inclusion of CWIP in rate base was in the public interest because it achieved a suitable balance between the utilities' need to recover costs in a more timely manner with the Commission's cost responsibility principles and lessened the rate impact of new transmission projects on customers.[12]

19. The Commission, however, has established certain conditions that must be met before it will approve the inclusion of CWIP in rate base.[13] Commission staff and intervening parties must be able to review the prudence of the construction costs that will be included, including the ability to compare the costs of alternative plans. In this regard, we find that NU has made a sufficient demonstration that these four major transmission projects are necessary to improve reliability in SWCT. They have been undertaken pursuant to ISO-NE's regional transmission expansion planning process in order to improve regional reliability, are intended to help resolve a number of electrical problems in SWCT, and to improve compliance with national and regional reliability standards.

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[9] *Construction Work in Progress for Public Utilities; Inclusion of Costs in Rate* Order No. 298, 48 Fed. Reg. 24,323 (June 1, 1983) *FERC Statutes and Regulations, Regulation Preambles 1982-1985* ¶ 30,455 (1983), *order on reh'g*, Order No. 298-B, 48 *Fed. Reg.* ¶ 31,092 (2000), *petitions for review dismissed, Public Utility District No. 1 of Snohomish County v. FERC*, 272 F.3d 607 (D.C. Cir. 2001) (Order No. 298).

[10] *Boston Edison Co.*, 109 FERC ¶ 61,300 (2004) (*Boston Edison*).

[11] *Id.* At P 29.

[12] Order No. 298 at 30,497.

[13] *Boston Edison*, 109 FERC ¶ 61,300 at P 33.

Further, each has been granted siting approval by the State of Connecticut following a comprehensive review process for each project.

20. As part of the condition for approval of CWIP treatment, a company must also propose accounting procedures that ensure that there is no duplicate recovery of CWIP and corresponding AFUDC. NU has submitted testimony and exhibits demonstrating that there will not be any duplicate recovery of any capitalized AFUDC that is related to the portion of CWIP included in rate base.[14]

21. NU seeks waiver of section 35.25(c) (4), which requires the submittal of estimated allocation ratios reflecting the anticipated use that wholesale customers will make of its system. NU states that its proposed allocation of CWIP is based on actual usage and that its formula rate contains a true-up provision for both costs and loads applicable to the CWIP component. Further, NU states that it will refund any differences between projected and actual data, with interest, pursuant to Commission regulations. As in *Boston Edison*, NU has in place a mechanism to ensure that allocators of CWIP are based on actual usage. In *Boston Edison*, the filing company already had a mechanism in place that assured the Commission that allocators of CWIP were based on actual wholesale customer usage.[15] Thus, in that case, the Commission waived requirements set in Order 298 for the use of estimated allocation ratios. Similarly, we will grant NU's requested waiver. However, we will require NU to ensure that customers who have paid for CWIP through its inclusion in rate base and who are not ultimately responsible for these facility costs will receive appropriate refunds, with interest.

22. We agree with NU that Unitil's concerns are premature, and that Unitil will have an opportunity to comment before NU charges customers for Category B (localized) costs.

23. In conclusion, we find that NU has made a sufficient showing that its proposed inclusion of 50 percent of CWIP in rate base is reasonable and in accordance with the Commission's requirements. Therefore, we will permit NU to include 50 percent CWIP in its rate base for the four construction projects discussed herein. In accordance with the requirement established in *Boston Edison*,[16] NU has pledged to submit an annual report with information as to the amounts of CWIP recorded for each of the SWCT projects, including related accounts such as AFUDC, and the resulting effect on the CWIP revenue

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[14] See NU's Exhibit NU-4 at p 7, and Exhibit NU-5.

[15] *Boston Edison*, 109 FERC ¶ 61,300 at P 38.

[16] *Id.* at P 33.

requirement. We will also require that NU's annual report provide the current status of each of the projects and their estimated or actual in-service dates.

The Commission orders:

NU's proposal to include 50 percent CWIP in rate base is hereby accepted effective February 1, 2006, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.