

BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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IN THE MATTER OF: :
CONSENT MARKETS, TARIFFS AND RATES - ELECTRIC :
CONSENT MARKETS, TARIFFS AND RATES - GAS :
CONSENT ENERGY PROJECTS - MISCELLANEOUS :
CONSENT ENERGY PROJECTS - CERTIFICATES :
DISCUSSION ITEMS :
STRUCK ITEMS :
- - - - -x

921ST COMMISSION MEETING
OPEN SESSION

Commission Meeting Room
Federal Energy Regulatory
Commission
888 First Street, N.E.
Washington, D.C.

Thursday, July 19, 2007
10:10 a.m.

921st Commission Meeting - Open Session
July 19, 2007

1 APPEARANCES:

2 COMMISSIONERS PRESENT:

3 CHAIRMAN JOSEPH T. KELLIHER (Presiding)

4 COMMISSIONER SUEDEEN G. KELLY

5 COMMISSIONER MARC SPITZER

6 COMMISSIONER PHILIP MOELLER

7 COMMISSIONER JON WELLINGHOFF

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1 P R O C E E D I N G S

2 (10:10 a.m.)

3 CHAIRMAN KELLIHER: Good morning. This open
4 meeting of the Federal Energy Regulatory Commission will
5 come to order to consider the matters which have been duly
6 posted in accordance with the Government in the Sunshine Act
7 for this time and place.

8 Please join us in the Pledge of Allegiance.

9 (Pledge of Allegiance recited.)

10 CHAIRMAN KELLIHER: Thank you for coming today.
11 We have an impressive agenda, I think.

12 We're actually exercising our jurisdiction across
13 the board, and we have some oil pipeline for those in the
14 oil pipeline bar, so you should be happy, as well.

15 And we're making a lot of policy today. We have
16 four NOPRs on the agenda, and we have two policy statements,
17 as well as a lot of other items.

18 But let's -- before we turn to the consent
19 agenda, I just want to make an announcement about an
20 important proposal the Commission has, that those of you who
21 are interested in hydro issues, will find interesting, I
22 think.

23 Namely, I would like to announce an important
24 proposal, an important proposed change in Commission policy
25 with respect to licensing new hydropower technologies.

1 Last December, as you know, the Commission held a
2 technical conference on the hydrokinetic technologies that
3 would use the force of waves, tides, and currents, to
4 generate electricity.

5 Now, these technologies have very significant
6 potential, but there are barriers to these technologies.
7 There are financial barriers, there are regulatory barriers,
8 there's technological barriers.

9 But really the principal barrier to the
10 development of these technologies, may be that at this
11 point, they are as yet unproven, not just in the United
12 States, but in the rest of the world, and that these
13 technologies must be proven before large-scale commercial
14 development can take place.

15 Now, the Commission has taken some steps to
16 improve -- to demonstrate, to prove these technologies.
17 We've shown a lot of flexibility in the Verdant Order, and
18 that pilot project is operating or collecting some useful
19 data.

20 But today we're proposing a major step to reduce
21 the regulatory barriers to the success of these new
22 technologies, and we're doing so in a way that promotes
23 exactly what is most needed, namely, pilot projects to
24 demonstrate these new technologies.

25 After the technical conference, I directed the

1 Commission Staff to determine whether the Commission could
2 establish a simplified licensing process suitable to license
3 pilot projects to demonstrate these new technologies, and
4 one that we could establish under our current legal
5 authority.

6 I am pleased to report that the Commission Staff
7 has responded with a very creative proposal to establish an
8 effective pilot project licensing process.

9 I just want to express my pride in the
10 Commission Staff for the creative proposal that they have
11 established. I also want to thank Woodrow Wilson and the
12 Congress of 1920, because I think it's quite impressive that
13 the 1920 Water Power Act is flexible enough to allow us to
14 achieve -- to explore the potential of technologies that
15 didn't exist at the time.

16 Now, the pilot project license that we're
17 proposing, would be available for projects that meet certain
18 criteria, namely, small projects of five megawatts or less;
19 projects that are removable or able to be shut down on
20 relatively short notice, in order to guard against
21 environmental harm; projects that are not located in waters
22 with sensitive designations; and, four, projects that would
23 be licensed for the purpose of demonstrating new
24 technologies or determining appropriate sites for ocean wave
25 and tidal energy projects.

1 Now, we would envision these licenses having a
2 short term of perhaps five years, and at the end of that
3 pilot license, developers would have two options: They
4 could apply for a standard license or they can decommission
5 and restore the site.

6 The pilot project license would include standard
7 safeguards that will allow the Commission to alter
8 operations or halt operations, to prevent unacceptable
9 environmental harm.

10 Now, we will release materials regarding the
11 proposed pilot project license, through the Commission's
12 website, and I do want to emphasize that this pilot license
13 can be granted under current law, without a change in
14 Commission Regulations.

15 So, in other words, we do have the ability to
16 issue pilot licenses in the immediate future.

17 However, it's clear that the success of this new
18 pilot project license, depends on the cooperation of other
19 federal and state agencies. For the pilot license to work,
20 it will be necessary for federal and state agencies to
21 identify the necessary environmental studies, early in the
22 process, and to issue any necessary permits in due course.

23 Now, from my point of view, it stands to reason
24 that the potential impact of a pilot project authorized to
25 operate under five years, under conditions that allow the

1 Commission to halt operation, if there's unacceptable
2 environmental impact, is quite different from the impact of
3 a large-scale project licensed to operate over a half
4 century.

5 And for that reason, I would hope that the scope
6 and environmental studies necessary to issue pilot licenses,
7 would be much reduced.

8 Now, the Commission plans to hold a technical
9 conference in October to explore the issues related to the
10 new pilot license proposal, and we will hold this conference
11 in the Pacific Northwest, where there is a great deal of
12 interest in these new technologies.

13 I have asked our colleague, Commissioner Phil
14 Moeller, to lead this technical conference, recognizing his
15 interest and knowledge in this area, and the fact that he's
16 the hometown kid from the Pacific Northwest, so, a double
17 benefit.

18 Now, the Commission is committed to removing
19 barriers to the development of these new hydropower
20 technologies. We've demonstrated flexibility in the past,
21 and now we offer a new pilot license that is carefully
22 tailored to promote technological demonstrations, while
23 guarding against environmental harm.

24 And I don't usually admit to being excited about
25 Commission proposals, and I am excited frequently about our

1 proposals, but I think we should be sober people here at the
2 Commission, but I will admit, as a hydro Commissioner, I'm
3 excited about this proposal today.

4 With that, I would like to recognize
5 Commissioner Moeller.

6 COMMISSIONER MOELLER: Thank you, Mr. Chairman,
7 and thank you for your effort and that of the Staff in
8 coming up with this proposal.

9 As I think most people know, there is a lot of
10 enthusiasm, particularly in the coastal states, but not
11 exclusively, for the new hydropower technologies, and yet we
12 have a bit of a chicken-and-egg issue in the current
13 licensing process, in terms of getting these rolling.

14 This is emission-free technology, which I think
15 in almost every case, would meet state renewable portfolio
16 standards, which are rather aggressive in the West, and we
17 want to take advantage of the enthusiasm now, and I look
18 forward to our conference in October, and certainly would
19 hope that I'd be joined by not only fellow Commissioners,
20 but anyone here who is interested in getting on the new wave
21 of hydrotechnology.

22 (Laughter.)

23 CHAIRMAN KELLIHER: Colleagues? Jon?

24 COMMISSIONER WELLINGHOFF: Thank you, Mr.
25 Chairman. I, too, am very excited about this, I really am.

1 This is a very exciting prospect.

2 I would like to thank Mark Robinson's staff and
3 all of the other Staff in the Commission that worked on this
4 pilot licensing proposal.

5 I think it's very important. I understand that
6 just in the Puget Sound area, there may be over two
7 gigawatts potential energy, a tremendous amount of potential
8 there to mine out of an area that obviously is a very high-
9 load area, as well, so you have it close to load center.
10 There are great opportunities there.

11 I have already offered to Commissioner Moeller to
12 assist in any way, I certainly plan on attending the
13 conference.

14 CHAIRMAN KELLIHER: Thank you. Commissioner
15 Kelly?

16 COMMISSIONER KELLY: Well, I think it is
17 exciting, because it's rare that you're at the beginning of
18 an emerging energy source, and that's where we find
19 ourselves.

20 I think that's one of the reasons it is
21 exciting. On the one hand, it might sound a bit
22 futuristic, this technology; on the other hand, we see here
23 at FERC, that it's very real.

24 We have received 57 preliminary permit
25 applications in the last three years, and as Jon mentioned,

1 a lot of energy is available to be harvested by this source,
2 and some estimates suggest that it could double the hydro
3 output of the U.S.

4 I think what we've been facing here and what
5 Staff on the ground has observed and has helped us
6 appreciate, is that there are two things we need to be
7 thinking about: How do we move this technology forward and
8 come to understand what it actually can do in the field,
9 while at the same time, understand what the environmental
10 impacts are of it?

11 I think that's what this pilot process works to
12 do, and that's our goal of accomplishing both.

13 I want to add to the Chairman's compliments to
14 the Staff for coming up with this.

15 CHAIRMAN KELLIHER: Thank you. Commissioner
16 Spitzer?

17 COMMISSIONER SPITZER: Thank you, Mr. Chairman.

18 First, the developers are sorely in need of a
19 regulatory framework in which to operate, and so I think you
20 have acknowledged that we're part of the solution to the
21 regulatory framework -- not the totality of the solution,
22 but the moving forward with that agenda is essential.

23 This is very creative and I compliment the
24 Chairman and the Staff for coming up with a very creative
25 and innovative means to achieve the regulatory framework.

1 Now, I hope that other federal agencies,
2 particularly state and local governments, will seek to move
3 forward. The areas we're discussing, tend to be
4 constrained, and so that's an additional benefit of this.

5 The East Coast, I know, and New England, New York
6 City, are vitally in search of additional supplies.

7 In terms of the anecdote, I was at a conference a
8 number of years ago. I think I had just been elected to the
9 Commission in Arizona, and this issue was being discussed,
10 and the developer was passionate and really got his audience
11 involved.

12 And it was basically who can argue with the
13 transcendent power of the moon? And I got up and said that
14 I have no interest in challenging the transcendent power of
15 the moon and tidal power, but it is just an enormous
16 opportunity, and one that the filing of -- I think that
17 Commissioner Kelly mentioned 57 applications -- is
18 reflective of the great interest in this new technology.
19 I'm very pleased to support this.

20 CHAIRMAN KELLIHER: And we look forward to the
21 technical conference, and we'll have a broad cross section
22 of people involved, and we certainly want the involvement of
23 sister federal agencies, as well as state agencies, as well
24 as the industry.

25 Now, with that, before we turn to the consent

1 agenda, I'd like out what I usually point out, which is how
2 many notationals we've issued since the last open meeting,
3 and the Commission, since the June 21st open meeting, has
4 issued 79 Notational Orders.

5 That's roughly 20 a week, roughly four a day,
6 every day since last June, and I want to commend the Staff
7 and I want to commend the advisors for all their hard work,
8 as well as my colleagues, to maintain that level of
9 production in between our open meetings.

10 With that, Madam Secretary, let's turn to the
11 consent agenda.

12 SECRETARY BOSE: Good morning, Mr. Chairman, good
13 morning, Commissioners. Since the issuance of the Sunshine
14 Act Notice on July 12th, E-15 has been struck from this
15 morning's agenda.

16 Your consent agenda for this morning, is as
17 follows: Electric Items - E-4, E-5, E-6, E-9, E-10, E-12,
18 E-13, E-14, E-16, and E-17.

19 Miscellaneous Item: M-1.

20 Gas Items: G-3, G-4, G-6, G-7, G-8, G-9, and G-
21 10.

22 Hydro Items: H-1, H-2, and H-3.

23 Certificate Items: C-1, C-2, and C-3.

24 Commissioner Moeller is not participating in
25 Consent Item E-9. As required by law, Commissioner Moeller

1 is not participating in Consent Item E-10. Also as to E-10,
2 Commissioner Kelly is concurring with a separate statement.

3 As to E-16, Commissioner Moeller is concurring,
4 in part, and dissenting, in part, with a separate statement.

5 We will now take a vote on the consent agenda
6 items for this morning, beginning with Commissioner
7 Wellinghoff.

8 COMMISSIONER WELLINGHOFF: I vote aye.

9 SECRETARY BOSE: Commissioner Moeller?

10 COMMISSIONER MOELLER: I vote aye, with the
11 exception of E-9 and E-10, noting my dissent and concurrence
12 in E-16.

13 SECRETARY BOSE: Commissioner Spitzer?

14 COMMISSIONER SPITZER: I vote aye.

15 SECRETARY BOSE: Commissioner Kelly?

16 COMMISSIONER KELLY: Aye, noting my concurrence
17 in E-10

18 CHAIRMAN KELLIHER: Chairman Kelliher?

19 CHAIRMAN KELLIHER: Aye. Madam Secretary, why
20 don't we turn to the discussion agenda?

21 SECRETARY BOSE: The first item for discussion,
22 only, is H-2, Project No. 12685-000. John Katz from the
23 Office of the General Counsel is available for questions.

24 CHAIRMAN KELLIHER: Commissioner Moeller?

25 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

1 This has to do with a hydro project that's located near
2 Puget Sound, actually pretty close to Takoma, and it's a
3 relatively controversial project, in the sense that there
4 were some Endangered Species Act issues.

5 It's been going on for a good ten years, and Jon,
6 can you kind of explain a little bit, what we're doing here?

7 MR. KATZ: Yes, what we're doing in this
8 instance, is issuing a preliminary permit for a developer to
9 study the project in question.

10 Some folks commenting in the case, indicated that
11 they had concerns about the possible impact of a project
12 upon other plans for the area and for the facilities in the
13 area, and the Commission is not, in issuing a preliminary
14 permit, in any way affecting the possibility of whatever
15 plans entities holding rights in the area, might have.

16 It's merely giving a developer the opportunity to
17 look into whether he might, in the future, want to file a
18 license application.

19 But, by doing that, the developer gets no
20 property rights or other particular rights in the site,
21 other than that no one else can file for a development
22 application during the pendency of his permit.

23 COMMISSIONER MOELLER: To put a little context,
24 there was an existing project, but it retains its
25 characteristics of the dam to keep the reservoir going, but

1 the power is no longer being generated there, correct?

2 MR. KATZ: That's correct; that is the current
3 situation there, yes.

4 COMMISSIONER MOELLER: And a lot of the affected
5 parties have come together. This is likely to stoke their
6 interest, I suppose, which is one of the reasons I've asked
7 to clarify some of these issues.

8 We grant a request for a permit here, as you
9 noted. Can you give examples of situations where the
10 Commission has actually denied a permit?

11 MR. KATZ: Certainly. For about two decades, the
12 Commission had a policy that it issued permits regularly,
13 unless there was a permanent legal bar to a project being
14 located in the site.

15 An example of that would be, for example, if
16 someone proposed a project or to study a project under a
17 preliminary permit on a stretch and wild and scenic river.
18 Under the Wild and Scenic Rivers Act, the Commission can't
19 license a project, so the Commission, in that instance,
20 would not issue a permit and would say there's a permanent
21 bar; we never could license this, so there's no point in
22 letting you study it.

23 In all other instances, even where parties
24 presented possible arguments against whether the project was
25 in the public interest, or whether the developer had the

1 finances to develop a project, the Commission said, we'll
2 look at those as relevant, at such time as the development
3 application comes before us, but the permit process is
4 designed for folks to think about projects and to look at
5 projects, so those issues are premature at that point.

6 Over the last few years, the Commission has
7 crafted a few very limited exceptions to that policy: One
8 came in a couple of instances where a preliminary permit
9 application was filed for a site which had been studied and
10 Commission Staff had issued an environmental document in the
11 context of an earlier license application.

12 And in that earlier proceeding, Commission Staff
13 had recommended against issuing a license, because of the
14 environmental impact on the site. So when later permits
15 came for that site, the Commission said, look, since Staff
16 has already said that the environmental impacts are not
17 worth a project, we're not going to issue a permit to study
18 that project.

19 There are two other instances in which we've
20 denied preliminary permits recently: One was -- or a couple
21 of them, similar cases -- were instances where the
22 Commission had determined in other proceedings, that the
23 proposed permit-holder was not a fit licensee, due to having
24 accrued civil penalties that weren't paid and other problems
25 in earlier proceedings.

1 There, the Commission said, okay, we will at this
2 time look at the fitness of that person and not issue them a
3 permit.

4 The other instances involved two cases where
5 developers had held licenses for the project site that was
6 proposed for the preliminary permit, and, over a decade or
7 more, had not developed the project, and the Commission
8 said, look, we don't want to get a preliminary permit
9 immediately from someone who has failed to develop the
10 project; let's see if anyone else out there wants to develop
11 it, but it would be a useless exercise to tie up the site
12 again for three years for someone who failed to develop a
13 project.

14 So those are the limited exceptions that the
15 Commission has made to its general policy.

16 COMMISSIONER MOELLER: One last question. In
17 February, we had the Notice of Inquiry on the new
18 hydrotechnologies, and we put the idea out there of a
19 strict-scrutiny approach when reviewing a permit request.

20 Did we get comments on that proposal?

21 MR. KATZ: Yes, we received on the order of 30
22 comments, and, out of those comments, I think maybe 27 of
23 them supported the strict-scrutiny approach, and the ones
24 that didn't favored, I think, not issuing preliminary
25 permits for offshore projects at all, so the overwhelming

1 weight of the comments was in support of the approach the
2 Commission selected, the strict-scrutiny approach.

3 COMMISSIONER MOELLER: All right, thank you.

4 CHAIRMAN KELLIHER: Thank you. Shall we vote?
5 Oh, we did? So we're discussing a consent item, thank you
6 for that.

7 Why don't we turn to --

8 SECRETARY BOSE: The remaining discussion items?

9 CHAIRMAN KELLIHER: Yes, the remaining
10 discussion items.

11 SECRETARY BOSE: The next items for discussion
12 this morning, are E-1, E-2, and E-3. They are involving
13 matters concerning Section 203 of the Federal Power Act.

14 We will have a presentation by Roshini
15 Thayaparan from the Office of the General Counsel, and
16 Valerie Kait from the Office of Energy Markets and
17 Reliability. They are accompanied by David Hunger --

18 CHAIRMAN KELLIHER: Madam Secretary?

19 SECRETARY BOSE: Yes?

20 CHAIRMAN KELLIHER: I don't have H-2 on my
21 consent list. Is it on the consent list that we -- it is.

22 SECRETARY BOSE: Yes, it is.

23 CHAIRMAN KELLIHER: Thank you.

24 SECRETARY BOSE: They are accompanied by David
25 Hunger and Andy Mosier, Office of Energy Markets and

1 Reliability, and Carla Urguhart, from the Office of the
2 General Counsel.

3 MS. THAYAPARAN: Mr. Chairman and Commissioners,
4 good morning. My name is Roshini Thayaparan, and I'm with
5 the Office of the General Counsel. With me this morning are
6 Carla Urguhart, also from the Office of the General Counsel,
7 and David Hunger, Valerie Kait, and Andrew Mosier from the
8 Office of Energy Markets and Reliability.

9 Kelly Perl, from the Office of Energy Markets and
10 Reliability, and Stewart Fischer from the Office of
11 Enforcement, also contributed to Items E-1, E-2, and E-3.

12 Items E-1, E-2, and E-3, are three related
13 actions designed to provide greater clarity and guidance on
14 the Commission's merger and corporate review policies, while
15 ensuring ratepayer protection against unauthorized cross
16 subsidies of utility and non-utility affiliates.

17 These items are based on the Commission's
18 experience since amending its regulations under Section 203
19 of the Federal Power Act, and enacting new regulations under
20 the Public Utility Holding Company Act of 2005.

21 These items are also the result of discussions at
22 the two technical conferences held in December 2006, and
23 March 2007, on these issues.

24 All of these actions are an outgrowth of the
25 Commission's implementation of the Energy Policy Act of

1 2005.

2 Item E-1 is a Draft Supplemental Policy
3 Statement providing guidance regarding future
4 implementation of Section 203. The Draft Policy Statement
5 complements, but does not replace the Commission's existing
6 policies set forth in the 1996 Merger Policy Statement.

7 Item E-1 addresses several issues: First, the
8 Policy Statement discusses the Commission's concerns
9 regarding inappropriate cross-subsidization and the pledge
10 or encumbrance of utility assets under Section 203(a)(4).

11 Section 203 applicants must provide a detailed
12 explanation of why their proposed transaction does not raise
13 such cross-subsidization concerns. This showing must be
14 made in Exhibit M of a Section 203 application.

15 The Policy Statement proposes three safe
16 harbors, that is, classes of transactions that are unlikely
17 to raise cross-subsidization concerns, so a detailed showing
18 under Exhibit M, will no longer be required.

19 These safe harbors include: Transactions where
20 no franchised public utility with captive customers is
21 involved; transactions that comply with specific state
22 regulatory protections against inappropriate cross-
23 subsidization; and transactions where a public utility
24 transacts only with non-affiliated entities.

25 The Policy Statement also provides that the

1 Commission will defer to state-adopted cross-subsidization
2 protections such as ring-fencing measures.

3 Further, while recognizing that cross-
4 subsidization protections must be implemented on a case-by-
5 case basis, the Policy Statement provides examples of ring-
6 fencing mechanisms that might be appropriate, depending on
7 the circumstances presented.

8 Second, the Policy Statement discusses the
9 requests for additional generic blanket authorizations under
10 Section 203(a)(1) and Section 203(a)(2).

11 While the Policy Statement explains why several
12 of the requested generic blanket authorizations would not be
13 appropriate at this time, Item E-3 proposes an additional
14 blanket authorization under Section 203(a)(1).

15 Third, the Policy Statement provides guidance
16 regarding what constitutes a disposition of control under
17 Section 203(a)(1). The Policy Statement affirms the
18 Commission's longstanding position that the disposition of
19 control is a fact-specific analysis.

20 However, the Policy Statement discusses the
21 Commission's existing precedent and provides additional
22 guidance.

23 In particular, the Policy Statement provides that
24 the Commission's general policy in future cases, will be to
25 presume that a transfer of less than ten percent of a public

1 utility's holdings, will not be considered a transfer of
2 control, if: One, after the transaction, the acquirer and
3 its affiliates and associate companies, directly or
4 indirectly, in aggregate, will own less than ten percent of
5 such public utility.

6 Two, the facts and circumstances do not indicate
7 that such companies would be able to directly or indirectly
8 exercise a controlling influence over the management or
9 policies of the public utility.

10 Again, the Commission will apply this policy on a
11 case-by-case basis.

12 Fourth, the Policy Statement discusses the
13 Commission's Appendix A analysis, which is used in assessing
14 a merger's effect on competition in wholesale electric
15 markets.

16 The Policy Statement explains that the
17 Commission will continue to use the analytical screens
18 adopted in the 1996 Merger Policy Statement, to help
19 identify mergers that have the potential to harm
20 competition, but that the Commission's review goes beyond
21 those screens and looks at all relevant factors regarding
22 the effect on competition.

23 The Commission will continue to analyze both
24 horizontal and vertical mergers by focusing on the merger's
25 effect on the company's ability and incentive to exercise

1 market power.

2 Next, Varlerie Kait will give a presentation on
3 Items E-2 and E-3.

4 MS. KAIT: Item E-2 is a Draft Notice of
5 Proposed Rulemaking or NOPR, proposing to codify cross-
6 subsidy pricing restrictions on power and non-power goods
7 and services transactions between franchised public
8 utilities with captive customers and their market-regulated
9 power sales affiliates or non-utility affiliates.

10 The proposed Rule expands the transactions and
11 entities to which these restrictions apply, in order to
12 protect against inappropriate cross-subsidization of market-
13 regulated and unregulated activities.

14 These restrictions would set forth uniform
15 affiliate transaction restrictions that overlap those
16 imposed by the Market-Based Rate Final Rule and imposed in
17 mergers since the enactment of the Energy Policy Act of 2005
18 that fill gaps in coverage.

19 Specifically, the proposed affiliate
20 restrictions would: First, require the Commission's
21 approval of all power sales by a franchised public utility
22 with captive customers, to a market-regulated power sales
23 affiliate.

24 Second, they would require a franchised public
25 utility with captive customers, to provide non-power goods

1 and services to a market-regulated power sales affiliate, or
2 non-utility affiliate, at a price that is the higher of cost
3 or market price.

4 Third, they would prohibit a franchised public
5 utility with captive customers, from purchasing non-power
6 goods or services from a market-regulated power sales
7 affiliate or non-utility affiliate, at a price above market
8 price, with the following exception: They would also
9 prohibit a franchised public utility with captive
10 customers, from receiving non-power services from a
11 centralized service company, at a price above cost.

12 Item E-3 is a Second Draft NOPR proposing to
13 codify a limited blanket authorization under Section
14 203(a)(1). Under the limited blanket authorization, a
15 public utility could, without prior Commission
16 authorization, dispose of less than ten percent of its
17 voting securities to a public utility holding company, only
18 if, after the disposition, the holding company and any
19 associate company, will own, in the aggregate, less than ten
20 percent of the public utility.

21 The Draft Order states that a disposition of such
22 limited voting interest, that is, less than ten percent,
23 with the proposed in-aggregate restriction and the existing
24 reporting requirements applicable to holding companies, will
25 not harm competition or captive customers and will

1 accommodate additional investment and market liquidity in
2 the electric industry.

3 This concludes our presentation. We will be
4 happy to respond to any questions that you might have.
5 Thank you.

6 CHAIRMAN KELLIHER: Great. Thank you very much.
7 I want to commend the Staff for their work on the package of
8 Orders.

9 I think they are really interesting, and I really
10 commend the Policy Statement, in particular, to the reading
11 of people on the outside, and I want to thank Cindy
12 Marlette, as well.

13 You know, there's word association games, and
14 203, to me, Cindy Marlette pops up, whenever I see 203.

15 (Laughter.)

16 CHAIRMAN KELLIHER: So, I just want to thank
17 Cindy for special attention to this package and really for
18 her leadership in bringing the package together.

19 Now, what we're doing today, as Staff indicated,
20 we're further implementing our expanded merger and corporate
21 review authority that Congress granted us two years ago in
22 the Energy Policy Act.

23 The Energy Policy Act significantly expanded the
24 Commission's authority in this area, granted us authority to
25 review holding company mergers, granted us authority to

1 review generation asset transfers.

2 It gave us a new responsibility to guard against
3 inappropriate cross-subsidization at the point of mergers,
4 and it also gave us new jurisdiction on securities, and we
5 have become a minor securities agency, due to the result of
6 the repeal of the Holding Company Act, as well as the 203
7 changes, and that's been an interesting growth area of
8 Commission work.

9 I thanked President Wilson earlier for the 1920
10 Federal Water Power Act, and I should thank Chairman
11 Bingaman for the merger provisions of the Merger Policy Act
12 of 2005. I think they really gave us the tools we needed in
13 this area.

14 The Commission moved quickly to implement the new
15 authority under the Energy Policy Act, and we're taking
16 additional steps today. I think it's important to point out
17 and stress that cross-subsidization is certainly not a new
18 responsibility for the Commission.

19 We've had it ever since the Federal Power Act of
20 1935. It's a basic aspect of ratemaking.

21 Normally, when we act to guard against cross-
22 subsidization, we're doing it when we're setting rates.
23 It's a little bit different to do so at the point of merger,
24 but it's certainly not a new area for the Commission.

25 Now, the package that we're approving today, does

1 strengthen protections against cross-subsidization. We're
2 codifying restrictions on affiliate transactions, we're
3 clarifying the mergers and acquisitions that raise
4 legitimate cross-subsidization issues and are, therefore,
5 subject to cross-subsidization protections, and we're also
6 providing guidance on what kinds of cross-subsidization
7 protections are appropriate, including ring-fencing.

8 I think these actions will provide greater
9 regulatory certainty on how the Commission will police
10 cross-subsidization. I think it's clear that not all 203
11 transactions raise legitimate cross-subsidization issues.
12 That's clear, based on our experience over the past two
13 years, and I think the Policy Statement does a good job of
14 identifying the universe of transactions that are
15 appropriately subject to cross-subsidization protections.

16 Now, we've also been careful not to taken an
17 expansive approach and not to preempt our state colleagues,
18 and I think the approach we're taking is respectful of state
19 authority.

20 We also facilitate certain securities
21 transactions by granting blanket approval from minor
22 dispositions of public utility securities to holding
23 companies, and it somewhat mirrors an approach on earlier
24 blanket authorization that we provided for securities
25 acquisitions by holding companies.

1 In my view, today's package completes our initial
2 implementation of rules that will govern future Commission
3 actions on 203 transactions, so I think it's a good package
4 and I support it.

5 Colleagues? Jon?

6 COMMISSIONER WELLINGHOFF: Thank you, Mr.
7 Chairman. I think that undue affiliate preference can
8 result in anti competitive market effects and higher costs
9 that harm consumers.

10 The Commission, though, uses a number of tools to
11 protect customers against those threats. I'm pleased to
12 support this package of Orders, which takes several steps to
13 protect customers against inappropriate cross-subsidization
14 between regulated utilities and unregulated affiliates.

15 Our Supplemental Policy Statement on Section 203
16 of the Federal Power Act, first recognizes that states have
17 an important role to play in protecting customers against
18 inappropriate cross-subsidization in the context of
19 corporate transactions.

20 But it also recognizes the authority on this
21 issue that Congress has assigned the Commission in EPAct
22 2005.

23 It makes clear that the Commission will take
24 action where state measures are inadequate to protect
25 wholesale customers. In addition, our Notice of Proposed

1 Rulemaking and Cross-Subsidization, would reinforce existing
2 Commission policy by codifying uniform affiliate
3 restrictions in our regulations.

4 And I would like to thank Staff for all the work
5 they did on these Orders. Thank you very much.

6 CHAIRMAN KELLIHER: Thank you. Colleagues?
7 Commissioner Kelly?

8 COMMISSIONER KELLY: It's almost been two years
9 since the Energy Policy Act was passed, and that statute
10 gave FERC a number of responsibilities, most of which we
11 were required to comply with in the first three months or
12 six months or year after the Act was passed.

13 And, under the Chairman's leadership, I am proud
14 to say that we met all of our deadlines, and I look at this
15 package of Policy Statement and NOPR, as really Phase II of
16 our implementation of the Energy Policy Act.

17 We have already established rules to implement
18 the new Section 203 of the Federal Power Act, and in doing
19 that, we provided for technical conferences to get more
20 input.

21 This package of Orders comes as a result of that.
22 I am pleased with the Policy Statement and I think that it
23 helps give more guidance to the industry about how the
24 Commission feels about cross-subsidization, and helps to
25 outline our view of the responsibilities that we share with

1 our state regulators.

2 I think that we have embarked on the right policy
3 with respect to ring-fencing.

4 E-2 is NOPR, which we propose that not only
5 applies to Section 203, but is much broader. I think it's a
6 good proposal.

7 It will apply standards of conduct for affiliate
8 transactions, now, to all traditional public utilities.
9 Currently, we have standards of conduct in place, we put
10 them in place on a case-by-case basis under 203; we have
11 them in place on a case-by-case basis in situations where
12 utilities apply for market-based rates, and so they exist
13 out there, but they are a result of circumstances.

14 And what this does, is rationalize those
15 standards of conduct and makes them applicable across the
16 board, without discrimination, to all traditional public
17 utilities that engage in transactions with their affiliates.

18 And that came about, actually, as a result of
19 comments of specific participants in our technical
20 conference, in particular, the American Public Power
21 Association and the National Rural Electric Cooperative
22 Association, who first suggested this at the conference we
23 held last December.

24 Also at our technical conference, we received
25 comments about facilitating disposal of public utility stock

1 in a more efficient way, and we act today in E-3, I think,
2 correctly, to provide for a limited blanket authorization
3 under Section 203 of the FPA, to allow a public utility to
4 dispose of less than ten percent of its voting securities,
5 to a public utility holding company, if, after the
6 disposition, the holding company and any associate company,
7 in the aggregate, owns less than ten percent of that public
8 utility.

9 And I think this strikes an appropriate balance
10 between facilitating the efficient functioning of the
11 markets and also providing consumer protection.

12 CHAIRMAN KELLIHER: Commissioner Moeller?

13 COMMISSIONER MOELLER: I just have a couple of
14 questions, actually.

15 CHAIRMAN KELLIHER: Certainly.

16 COMMISSIONER MOELLER: I'm not sure who they
17 should go to on the team, but have we addressed all the
18 outstanding issues in terms of what we were directed to do
19 now, out of EAct on this set of subjects, or is there
20 anything else?

21 MS. URGUHART: We have addressed most of them in
22 substance, at this point. The comments that we received in
23 the technical conferences earlier this year and the end of
24 last year, were very helpful to us to move forward in
25 providing these further clarifications.

1 MS. MARLETTE: If I could just add, we have
2 addressed everything that Congress directed us to. There
3 were certain things raised in the technical conferences,
4 like requests for additional blanket authorizations, and, I
5 think, some discussion about whether the Commission should
6 modify its current cash management policy.

7 But the Commission, in this draft, the Draft
8 Policy Statement, decides that it's not appropriate to do
9 additional generic authorization, other than the one that's
10 in the NOPR at this particular time, or take other action.

11 COMMISSIONER MOELLER: Although we're not
12 foreclosed from taking it?

13 MS. MARLETTE: Correct, correct.

14 COMMISSIONER MOELLER: Okay, thank you. Thank
15 you, Mr. Chairman.

16 CHAIRMAN KELLIHER: Just to follow up on that, I
17 think in this area, Congress gave us authority, but they
18 didn't direct us to how to implement the authority. In
19 other areas of EPAct, they said do a rulemaking with X-days,
20 so, we have the authority and we've implemented it at our
21 own discretion. Marc?

22 COMMISSIONER SPITZER: Thank you, Mr. Chairman.
23 It's interesting, how the process that unfolded, resulted in
24 some changes, specifically, those requested by the financial
25 community in the blanket authorizations.

1 Business models have changed over time,
2 government has not always been flexible in dealing with
3 changed circumstances, but this is one of those cases where,
4 in fact, the rules have been changed consistent with the
5 federal statute, and also mindful of the parties' comments
6 that were reflective of, again, the changed nature of the
7 energy sector of the economy.

8 One point I wanted to highlight, that has already
9 been discussed by my colleagues, is with regard to the
10 cross-subsidization. The Congressional enactment was
11 designed to fill a regulatory gap.

12 That gap was identified. There are
13 jurisdictions in which there is no state law in the area of
14 consumer protection with regard to cross-subsidization, and
15 so we have filled that regulatory gap.

16 But there was a potential for some mischief, I
17 think that's probably the correct term, where state ring-
18 fencing regulations that had been drafted in conformance
19 with state law, and in the view of those jurisdictions,
20 adequately provide consumer protections, could have been
21 preempted or even conflicted with, had the Commission not
22 taken the dexterous route of accommodating the state
23 interests.

24 I think we've done that, we've achieved that
25 objective. It was, frankly, a matter of concern during my

1 time on the state commission and among other state
2 commissioners, and I think we've achieved the purpose of
3 consumer protection, without provoking an unnecessary
4 conflict or exercising preemption in a manner that would
5 have been negative with regard to state interests.

6 That, again, speaks of this Commission, that we
7 found a very dexterous approach to fulfilling the intent of
8 Congress, and yet leaving undisturbed, very substantially,
9 well-thought-out, state ring-fencing provisions. We've done
10 that and we've succeeded, and I congratulate the Staff for a
11 good work product.

12 CHAIRMAN KELLIHER: Thank you. Any other
13 questions or comments?

14 (No response.)

15 CHAIRMAN KELLIHER: Let's vote.

16 SECRETARY BOSE: We will take a vote on these
17 items together, beginning with Commissioner Wellinghoff.

18 COMMISSIONER WELLINGHOFF: I vote aye.

19 SECRETARY BOSE: Commissioner Moeller?

20 COMMISSIONER MOELLER: Aye.

21 SECRETARY BOSE: Commissioner Spitzer?

22 COMMISSIONER SPITZER: Aye.

23 SECRETARY BOSE: Commissioner Kelly?

24 COMMISSIONER KELLY: Aye.

25 SECRETARY BOSE: Chairman Kelliher?

1 CHAIRMAN KELLIHER: Aye.

2 SECRETARY BOSE: The last item for discussion
3 this morning, is G-1, concerning the composition of proxy
4 groups for determining gas and oil pipeline return on
5 equity.

6 We will have a presentation by Richard Howe from
7 the Office of the General Counsel. He's accompanied by
8 Michael McLaughlin from the Office of Energy Markets and
9 Reliability.

10 MR. HOWE: Good morning, Chairman Kelliher and
11 Commissioners. My name is Richard Howe, and I'm in the
12 Office of General Counsel, and joining me today is Mike
13 McLaughlin from the Office of Energy Markets and
14 Reliability.

15 G-1 is a proposed Policy Statement concerning the
16 composition of the proxy group used to determine the return
17 on equity for both natural gas pipelines and oil pipelines
18 under the discounted cashflow method.

19 In recent years, there has been a decline in the
20 number of publicly-traded corporations with substantial
21 pipeline business, which are available for inclusion in the
22 proxy group. And firms engaged in the pipeline business,
23 are increasingly organized as master limited partnerships or
24 MLPs.

25 As a result, there are very few natural gas

1 pipelines that meet the Commission's traditional standards
2 for inclusion in the proxy group, and there are no oil
3 pipeline companies.

4 Under the proposed policy, the Commission would
5 permit MLPs to be included in the proxy group, however, the
6 Commission would cap the cash distribution used to determine
7 an MLP's return under the DCF method that the MLP has
8 reported earnings.

9 The Commission would also require a showing that
10 the MLP has had stable earnings over a multi-year period, so
11 as to justify a finding that it will be able to maintain the
12 current level of cash distributions in future years.

13 The proposed Policy Statement finds that these
14 requirements should render the MLP's cash distributions,
15 comparable to a corporation's dividend for purposes of the
16 DCF analysis.

17 Under the proposed policy, the Commission would
18 leave to individual cases, the determination of which
19 specific MLPs and corporations should be included in the
20 proxy group.

21 Finally, the Draft Policy Statement requests
22 comments on the proposed policy within 30 days of its
23 publication in the Federal Register, and provides for reply
24 comments within another 20 days. We would be happy to
25 answer any questions you may have.

1 CHAIRMAN KELLIHER: Thank you. I want to thank
2 Richard again and I'll probably want to embarrass you again
3 for a well-written Order. I enjoy reading your Orders, and
4 this one is a pleasure, as well, on a subject that some
5 people find very interesting.

6 (Laughter.)

7 CHAIRMAN KELLIHER: I suppose that if this were
8 fiction, it would be the mystery of the disappearing proxy
9 group. That would probably be a good title of a story.

10 (Laughter.)

11 CHAIRMAN KELLIHER: But today we're proposing a
12 significant policy change with respect to the composition of
13 proxy groups for determining returns on equity for natural
14 gas and oil pipelines.

15 And under the change, as Staff has indicated, we
16 would allow MLPs to be included in the proxy group for
17 calculation of returns under the DCF model.

18 Now, there is frequently the perception that
19 regulators introduce change into areas where there is
20 repose, and I don't think that's what we're doing here
21 today. We're reacting to change, pretty striking structural
22 changes that have occurred in both the oil pipeline and
23 natural gas pipeline sectors, and I think it's necessary
24 that we react to those changes.

25 Now, historically, the Commission has required

1 that companies in the proxy group meet certain standards.
2 One of those standards is that pipeline operations account
3 for 50 percent or more of the company's assets or income.

4 That standard has excluded many companies from
5 the proxy group, to the point where we actually had to make
6 adjustments. We have adjusted our historical approach,
7 based on the structural changes that have occurred in the
8 industry, but we're proposing a different approach today.

9 There is, frankly, no inherent problem with DCF
10 methodology; the problem is the disappearing proxy group.
11 We've gotten to the point where the policy question before
12 the Commission is, have we reached the tipping point?

13 Have we reached the point where so much of the
14 natural gas sector, in particular, has adopted the MLP
15 structure, that it's perverse for us to exclude MLPs from
16 the proxy group?

17 I think it's clear that we reached that point
18 some time ago with respect to oil pipelines.

19 Now, I had come to the belief that I think we
20 have reached the point where we should include MLPs in the
21 proxy group. I think it's time for the Commission's
22 ratemaking methodology to reflect the reality of the
23 industry structure that we are regulating.

24 And I think the real question before us, is how,
25 exactly, to go about doing that? Now, we offer a solution,

1 we propose a solution in the proposed Policy Statement, and
2 we seek comment.

3 The Commission has had longstanding concerns
4 about comparability between distributions and dividends, and
5 our solution takes a very deliberative approach towards
6 comparability, and we're careful.

7 We propose adjusting the amount of distributions
8 that will be included, and cap dividends at reported
9 earnings.

10 Now, from time to time, some of us on the
11 Commission have a special expertise that can be brought to
12 bear in some of our policy decisions. The resident chemist
13 came in very handy during our gas quality and
14 interchangeability policymaking, and that was very helpful.

15 I never understood the Periodic Table, but you
16 were very conversant with these matters, and that helped us
17 a great deal.

18 Now, we have a different expertise on this, with
19 respect to Marc Spitzer and his tax expertise, and I know
20 he's going to prove to be a great help as we move forward on
21 MLPs.

22 But, again, just to recap, from my point of view,
23 the question really is how to go about including MLPs in the
24 proxy group. I've reached the point where I think we have
25 to do it, but the question really is exactly how to do that.

1 We do have a proposed solution. We'll take
2 comments, and I'm sure people will offer different
3 approaches. But I do think the policy statement is the
4 right approach.

5 Colleagues? Commissioner Kelly?

6 COMMISSIONER KELLY: I agree with, Joe, and I
7 think that it's important to emphasize what we have changed
8 and what we haven't changed. And, as you explained, what
9 we're doing here, is allowing changes to the proxy group
10 that will now reflect reality and allow the inclusion of
11 MLPs, and I think that's a very good idea.

12 And we have some conditions on it, in order to
13 assure that there is no unintentional over-recovery in
14 rates, because of the difference in ways that MLPs make
15 payout dividends, versus other corporations.

16 And I think that that's also a good idea, and
17 I'll be interested in hearing the comments on that.

18 Also, as you mentioned, what we haven't changed,
19 is our general approach to determining an appropriate return
20 on equity, and I think that's because the DCF model, which
21 we have used, has stood the test of time.

22 It's been specifically approved by the Court of
23 Appeals, as an appropriate method to determining ROEs, and I
24 think what this proposed Policy Statement does, is show that
25 the DCF is, indeed, flexible enough to adjust to changed

1 circumstances, while at the same time, at the heart of the
2 analysis, is a reasoned approach to setting ROEs.

3 So, I'm pleased with our proposal here and look
4 forward to the comments from those who are concerned about
5 these issues.

6 CHAIRMAN KELLIHER: Commissioner Moeller?

7 COMMISSIONER MOELLER: Thank you, Mr. Chairman.
8 I first want to commend the decision to put this out as a
9 Draft Policy Statement. I'm hoping that it actually does
10 allow for a vigorous, although paper debate, as to where
11 we're going with this.

12 I think you're right that we have reached the
13 tipping point, and I'm glad we're addressing this, because
14 tax policy, I guess, really promoted through the '86 Act,
15 has led us to where we are with this disparate proxy group,
16 and yet when we make changes to our ratemaking policies
17 like this, it will have long-term effects for both the
18 industry and the ratepayers.

19 I hope we will get vigorous input from tax
20 experts, financial experts, consumer advocates, the
21 industry, and even those in academia, because there are
22 always pros and cons to making changes. Every financial
23 structure has pros and cons, and yet we don't make all this
24 policy in a vacuum.

25 If Congress decides to change the Tax Code, as

1 they will eventually -- maybe not specific to this -- we may
2 have to react, as well.

3 Again, I encourage and invite vigorous feedback
4 on this over the next 30 days. Thank you.

5 CHAIRMAN KELLIHER: Thank you. Commissioner
6 Spitzer?

7 COMMISSIONER SPITZER: Thank you, Mr. Chairman.
8 Let me make a few observations. I, too, am pleased that
9 this Policy Statement has been issued.

10 This area of FERC regulation is a bastion of
11 cost-of-service regulation, and, as always, the competing
12 interests to be balanced are the need for capital investment
13 with protection of the ratepayers through just and
14 reasonable rates.

15 In a matter back in October, I recall
16 Commissioner Wellinghoff making the comment that he had done
17 a lot of work over the years in cost of service regulation,
18 and the Commissioner's quote was, "It's more of an art than
19 a science," which means it is amenable to case-by-case
20 adjudications, uniquely so.

21 And I agree with that very much, yet the
22 industry requires some degree of reasonable certainty, and I
23 think the approach we've embarked upon, preserves the art of
24 determining case-by-case adjudications on just and
25 reasonable rates, with an overarching certainty in the area

1 of the law that the industry, I think, has demanded and is
2 entitled to.

3 I agree with my colleagues that the DCF model no
4 longer works, and the idea of arbitrarily restricting proxy
5 groups to C-corporations, I don't believe, has any basis in
6 law, and it certainly doesn't have any basis in the current
7 American economy.

8 The oil pipelines reached the point where the C-
9 corps are now a null set, so there's no alternative
10 whatsoever to changing the proxy group, and certainly the
11 trends in the gas pipeline industry are in favor of pass-
12 through groups.

13 I'll try and avoid the jargon from the tax
14 people, who have even worse jargon than normal human beings,
15 but the corporations that are organized under Subchapter (c)
16 are distinguished from S-corporations and other entities
17 that are taxed as partnerships, that pass through, and that
18 Subchapter (k) of the Code -- and the new investors --

19 You know, during the '70s, we had the rise of
20 mutual funds, and now we've got the hedge funds and the
21 infrastructure funds, and virtually all of these entities
22 are taxed under Subchapter (k) or not taxed, to be more
23 precise, and those are pass-through entities.

24 And even some of the mutual funds that were not
25 deemed tax efficient, have tried within the mutual fund

1 ambit, to be tax efficient, because the investors are
2 resistant to paying tax, particularly when you pay tax on
3 money that you do not receive. That tends to have unhappy
4 taxpayers.

5 So, this, again, as was pointed out, is a trend
6 in the industry, and where we were left in a prior decision
7 of this Commission, with an inability to use the Subchapter
8 (k) entities as proxies, resulted in an artificial adder to
9 achieve some degree of symmetry.

10 And, again, the use of an artificial adder,
11 really crystallized the argument in favor of a change in the
12 policy for the inclusion of MLPs.

13 I think that in terms of the policy arguments --
14 and I really appreciate, particularly, the comments of
15 Commissioner Moeller, on the need for infrastructure in this
16 country, generally.

17 Specifically, with regard to natural gas
18 pipelines, the huge cost differential and supply basins, the
19 fact that the percentage of retail rates attributable to
20 transportation, continues to decline, and the increasing
21 commodity prices pose a greater interest in these cost
22 differentials in the various supply basins, and then the
23 potential for carbon constraints means that natural gas is
24 going to be the bridge fuel to whatever source of fuel for
25 electricity the public policy of this country and the

1 economics of the industry ultimately arrives at, and
2 pipeline capacity is essential.

3 In working on this, Mr. Chairman, I've got to be
4 blunt. I always commend the Staff, and I will do so in this
5 case, for coming up with this Policy Statement, but in
6 reading the pleadings in other cases, I actually found them
7 to be unhelpful.

8 My tiny brain was confused.

9 (Laughter.)

10 COMMISSIONER SPITZER: But what I read from the
11 parties -- and it -- there was a sense of hyperbole in this
12 area in the litigated cases, that we'd have the end of the
13 world and the end of western civilization as we know it, if
14 ROEs were not in excess of 18 percent or the other parties,
15 nine or eight percent.

16 And the arguments made the idea of throwing in
17 the kitchen sink, was never an approach that I thought was
18 valuable, and in the years that I litigated against the
19 Federal Government, I just didn't think it was appropriate
20 to throw in really bad arguments.

21 I've seen lawyers use footnotes, with the idea
22 that if I have a really horrible argument that's just a
23 throwaway, maybe I'll put it in a footnote and maybe it
24 won't offend the tribunal.

25 (Laughter.)

1 COMMISSIONER SPITZER: I don't think that works.
2 And, from my point of view now, on the bench, I can assure
3 it doesn't work.

4 Subchapter (k) is now the rule for gas
5 pipelines. It's no longer the exception, and I agree with
6 the very well written Draft Policy Statement we have, the
7 conclusion of which is that the growth of earnings variable
8 in the DCF model, is one that could be isolated and dealt
9 with analytically.

10 So that leaves the sole unresolved issue as the
11 current dividend yield question. I note that C-corporations
12 redeem or repurchase stock, they issue new debt, they issue
13 hybrid stock, so in many circumstances, the issue of
14 retained earnings in C-corporation operations, is similar to
15 that of master limited partnerships, so I do believe this
16 is an issue that can be dealt with.

17 The resolution achieved in this document, is that
18 there be a cap on distributions in excess of earnings.
19 Although I did see expert testimony appear in pleadings, I
20 remain unconvinced that the absence of a cap on
21 distributions, would somehow --

22 I believe there's a double recovery, no matter
23 which way you slice it; that the consideration of a
24 depreciation in the general rate case, means that if we
25 don't cap these distributions, there is a windfall to the

1 pipeline.

2 The cap is designed to eliminate that double
3 recovery.

4 As the Policy Statement points out, the IBES
5 rating suggests the market responds to distributions in
6 excess of earnings, and there's a correction in that you've
7 got a circumstance where MLPs in the proxy group would have
8 perhaps higher current dividend yield than C-corporations,
9 generally, but the long-term earnings would be less than the
10 C-corporations.

11 So the market has achieved a rough equilibrium, a
12 rough equivalence that is consistent with traditional
13 ratemaking, and so I don't believe this is an exception to
14 traditional ratemaking principles. I believe it's a
15 correction and perfection of the ratemaking principles.

16 I draw some comfort from the recent decision at
17 the Court of Appeals in the ExxonMobil decision. I think
18 the tax issue has now been resolved with finality.

19 I agree with Commissioner Moeller that the
20 Internal Revenue Code section adopted by Congress in 1987,
21 Section 7704, expresses an intent of Congress to provide,
22 specifically, the opportunity for Subchapter (k) status for
23 this sector of the economy, and I think this Commission --
24 the courts certainly recognize the act of Congress, and I
25 think this Commission ought to also comport with

1 Congressional intent.

2 The law in that decision, was that there is no
3 legal principle, per se, that denies a tax allowance to a
4 pass-through entity. I think the similar law with regard to
5 the proxy groups, is the case.

6 So I think we -- I do look forward to additional
7 comments, but certainly in terms of balancing the competing
8 interests, I think this is the proper approach. I think the
9 ultimate ROEs in specific cases, will be consistent with
10 those that the Commission has granted in the past.

11 They will be consistent with the need for
12 additional capital investment in this sector of the economy,
13 and, at the same time, provide ratepayer protections.

14 Again, I point out that the cap on current
15 dividends, is designed to eliminate a potential double
16 recovery that would give higher ROEs than would otherwise be
17 justified by the law.

18 Then, where we have the flexibility to decide
19 these cases on a fact-specific basis, and yet provide, by
20 introduction of the MLPs, some certainty and guidance to the
21 industry, so, with that, I support this Order, and again
22 thank the Staff for a well written work product.

23 CHAIRMAN KELLIHER: Jon?

24 COMMISSIONER WELLINGHOFF: Thank you, Mr.
25 Chairman. I am certainly by no means a tax expert. I have

1 trouble doing my own taxes.

2 With respect to this particular proposed policy
3 statement, I do believe that, given the shifting financial
4 structure of the industry, it's appropriate, and I do
5 believe that the industry needs to make additional
6 investment.

7 I'm very interesting in how the industry is
8 making that investment, interested from the perspective that
9 I think that there is a tremendous amount of efficiency in
10 the interstate pipeline system that can be wrung out of it,
11 that's not yet being captured.

12 I hope that, in fact, that industry can invest in
13 a way that's more efficient in the future, so I'm very
14 interested in the comments, as Commission Moeller indicated,
15 and interested in the comments that will be made by the
16 industry to us with respect to this proposal, and I'm glad
17 we are sending it out for comment.

18 I'd like to really know from the industry, how
19 this proposed policy may impact the ability of the industry
20 to finance in the future, improvements to efficiency of the
21 pipeline structure. Thank you.

22 CHAIRMAN KELLIHER: Thank you. Any other
23 comments?

24 (No response.)

25 CHAIRMAN KELLIHER: No? Let's vote.

1 SECRETARY BOSE: The vote will begin with
2 Commissioner Wellinghoff.

3 COMMISSIONER WELLINGHOFF: I vote aye.

4 SECRETARY BOSE: Commissioner Moeller?

5 COMMISSIONER MOELLER: Aye.

6 SECRETARY BOSE: Commissioner Spitzer?

7 COMMISSIONER SPITZER: I vote aye.

8 SECRETARY BOSE: Commissioner Kelly?

9 COMMISSIONER KELLY: Aye.

10 SECRETARY BOSE: And Chairman Kelliher?

11 CHAIRMAN KELLIHER: Aye.

12 Now, we have a closed meeting today, and one of
13 us has a restriction on time. Can we start the closed
14 meeting at noon? Does that work for my colleagues? Noon?
15 Great.

16 Okay, let's start the closed meeting at noon, and
17 if we can clear the room of non-press guests, that would
18 help, and we'll have a press conference quickly. Thank you
19 very much.

20 (Whereupon, at 11:10, the Open Session was
21 concluded.)

22

23

24

25