Atlantic Path 15, LLC Docket Nos. ER08-374-001
EL08-38-001

ORDER GRANTING REHEARING IN PART, DENYING REHEARING IN PART,
AND DIRECTING COMPLIANCE FILING

(Issued November 18, 2010)

1. This order addresses the request for rehearing and clarification filed by
Southern California Edison Company (SoCal Edison) in response to the Commission’s
February 19, 2008 order, which addressed Atlantic Path 15, LLC’s (Atlantic) proposed
tariff change to decrease rates that it charges for transmission service over the
transmission line upgrade (Path 15 Upgrade) and related substation upgrades to the
Path 15 corridor financed by Atlantic. In the February 2008 Order, the Commission
accepted Atlantic’s proposal, suspended the rates for a nominal period, to become
effective on February 20, 2008, subject to refund, and established hearing and settlement
judge procedures. For the reasons discussed below, we will grant in part and deny in part
SoCal Edison’s request for rehearing of the February 2008 Order. Specifically, we
clarify that we are not mandating the use of regional proxy groups in this or other cases,
and also clarify that our decision to make an up-front return on equity (ROE)
determination will depend on the facts and circumstances of the individual cases.
Further, we grant rehearing of the February 2008 Order’s determination that accepted

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2 For purposes of this order, up-front ROE determinations include those situations
in which the Commission makes ROE determinations following a paper hearing process,
as well as situations in which the ROE determination is made on the basis of a review of
a party’s filing and any protests.
Atlantic’s use of a historical test year, and direct Atlantic to submit a compliance filing within 30 days of the date of this order.

I. **Background**

2. The Path 15 Upgrade is an 83-mile, 500 kV transmission line built along the existing Path 15 corridor in California to relieve a constrained congestion point. In 2001, the Commission specifically recognized the Path 15 corridor as a significant problem area requiring incentives for investment to alleviate costly congestion. The upgraded Path 15 transmission line went into operation on December 22, 2004, adding roughly 1,500 MW to the existing 5,400 MW of transmission capacity from southern to northern California, and increasing transmission capacity from north to south by about 1,100 MW. On November 20, 2006, the Commission found Atlantic’s proposed transmission revenue requirement (TRR) and transmission operator tariff to be just and reasonable, following certain modifications. Pursuant to an earlier settlement agreement, Atlantic agreed to file rate cases not more than three years apart, starting at the end of the first three-year rate period, and agreed that it would not seek an ROE in excess of 13.5 percent in the first rate case. The Commission allowed a three-year moratorium on rate filings and directed Atlantic to file a rate case at the end of the moratorium, including an updated (actual) capital structure for the company.

3. On December 21, 2007, Atlantic filed a proposal to reduce its TRR to $32,146,252, which would be a reduction of $2,774,782 from the current rates on file with the Commission (December 2007 Filing). The proposed TRR was based on the company’s actual capital structure of 52 percent debt and 48 percent equity and a test

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year consisting of the 12 months ended December 31, 2006. Atlantic requested continuation of its 13.5 percent ROE without suspension, hearing, or refund. Atlantic also sought Commission approval of the amortization in Account 181 (Unamortized Debt Expense) of $4,500,000 in costs incurred in arranging the upgrade project’s debt financing.

4. In the February 2008 Order, the Commission found that Atlantic’s proposed rate change (other than the requested 13.5 percent ROE and the use of a historical test year) raised issues of material fact and, accordingly, set the matter for hearing and settlement judge procedures. The Commission suspended Atlantic’s tariff revisions for a nominal period and permitted the rates to become effective February 20, 2008, subject to refund, and the outcome of the hearing. In addition, the Commission found that Atlantic’s use of a historical test year comported with section 35.13 of the Commission’s regulations.

5. The Commission also summarily approved Atlantic’s 13.5 percent ROE, and found that Atlantic’s use of the single step discounted cash flow (DCF) methodology was consistent with Commission policy. In doing so, the Commission discussed the benefits of using region-wide proxy groups for the determination of ROE, including the process by which such proxy groups can provide up-front certainty to the financial community regarding recovery of investments made in critical infrastructure. Specifically, the Commission explained that Atlantic’s proposed proxy group comprised 17 investor-owned utilities in the Western Electric Coordinating Council (WECC) footprint, where the Path 15 Upgrade is located. The Commission stated that Atlantic used appropriate screening parameters in its analysis, which reduced the number of companies in Atlantic’s proxy group to nine, with a range of reasonable returns of 7.63

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7 See December 2007 Filing at 5.
8 February 2008 Order, 122 FERC ¶ 61,135 at P 14.
10 February 2008 Order, 122 FERC ¶ 61,135 at P 16.
11 Id. P 15-16.
percent to 13.67 percent. Based on this WECC-wide proxy group, the Commission found that continuation of Atlantic’s 13.5 percent ROE was reasonable and consistent with the stated purpose of the recently-enacted section 219 of the Federal Power Act (FPA), the principles set forth in Order No. 679, and recent precedent. The Commission also found that, as a matter of policy, it was appropriate to use a proxy group with companies from the region in which the utility is located, with appropriate screening parameters, in calculating a ROE using the DCF method. The February 2008 Order also stated that use of a regional proxy group may allow for more up-front ROE determinations.

6. Subsequently, Atlantic and several parties entered into an uncontested settlement (Settlement) in this proceeding that resolved many of the issues that the Commission set for hearing. The Settlement also provided for the withdrawal of a request for rehearing filed by the California Public Utilities Commission (CPUC), but reserved the three issues raised by SoCal Edison in its rehearing request and established compliance obligations

13 Atlantic’s screening parameters included: (1) using only those utilities that are currently paying cash dividends; (2) using utilities that are covered by two generally recognized utility industry analysts; (3) using utilities that had similar senior bond and/or corporate ratings; (4) using utilities that had not announced a merger during the six-month period used to calculate the dividend yields; and (5) using utilities that have both a Thompson Financial First Call growth rate and are covered by Value Line. See February 2008 Order at P 20.


18 Id.
should the Commission grant rehearing on one or more of these issues. The Commission approved the settlement as fair and reasonable and in the public interest.¹⁹

II. Discussion

7. In its rehearing request, SoCal Edison argues that the Commission: (1) should not mandate the use of WECC-only regional proxy groups for utilities located in the western United States, excluding otherwise comparable non-WECC utilities in a proxy group used to determine the ROE for a WECC utility; (2) should not mandate use of an up-front ROE determination methodology in all incentives and general rate cases; and (3) erred in approving Atlantic’s use of a historical test year without setting the issue for hearing.

A. Regional Proxy Groups

1. Rehearing Requests

8. SoCal Edison states that, to the extent that the February 2008 Order holds that a region-wide proxy group must be used in all ROE cases for all utilities in the WECC, it seeks rehearing. Historically, SoCal Edison explains, the Commission has drawn from throughout the country to assemble a proxy group of comparable risk using several screening criteria in order to assemble that group, including bond rating, utility size, exposure to nuclear generation, and the absence of merger activity. It asserts that proxy groups are also typically determined based on the specific facts of each case and that imposing a one-size-fits-all proxy group standard would inappropriately limit the Commission’s ability to develop the criteria most appropriate for use in individual cases. SoCal Edison argues that the February 2008 Order represents the first time in which the Commission has indicated that it might require the exclusion of comparable non-western utilities from a proxy group, based solely on these utilities’ location outside the WECC, and thus represents a major change in policy with far-reaching consequences.

9. SoCal Edison submits that excluding from the proxy group otherwise comparable utilities located outside the WECC also distorts the DCF analysis by unduly limiting the sample. SoCal Edison points out that, unlike certain utilities and RTOs in other regions of the country where the Commission has used geographic proximity as a screening criterion, the utilities in the WECC have a wider range of risk factors that is more characteristic of the nation as a whole than of a distinct sub-region. It states that WECC members rely on markedly different portfolios of power supply resources, ranging from

¹⁹ *Atlantic Path 15, LLC*, 128 FERC ¶ 61,130 (2009). Although the CPUC did not file a formal request to withdraw its rehearing request, we deem that request withdrawn because we have approved the Settlement.
portfolios that are dominated by coal-fired generation, to portfolios that are dominated by hydroelectric or natural gas generation. SoCal Edison argues that the mere fact that western utilities are electrically integrated and operate in the same geographic area does not establish that they face comparable business or financial risks. Moreover, SoCal Edison points to Commission precedent where it rejected using geographic location as a proxy group screening factor. SoCal Edison also argues that limiting the proxy group to WECC utilities ignores the fact that utilities compete for scarce capital with companies around the nation, noting that the financial markets in which that competition occurs are not regional, but national or even international.

10. Further, SoCal Edison submits that using a national sample, with Atlantic’s screens, would provide the same measure of regulatory certainty and would be just as straightforward as using a region-wide sample. Thus, it argues that the Commission should adopt a national – not a region-wide – sample, screened with Atlantic’s criteria and reject the required use of a WECC-only proxy group.

11. Finally, SoCal Edison asserts that the Commission’s action in this case obscures the far-reaching impact of its decision to assemble a WECC-only proxy group, explaining that excluding non-WECC members from consideration in a DCF analysis would substantially lower both the top and midpoint of the range of reasonableness. SoCal Edison further notes that the reduction is not apparent here because Atlantic began with a WECC-only sample and because its incentive ROE request was acceptable so long as it was below the top of the range of reasonableness. SoCal Edison contends that the impact on the utility would be apparent in non-incentive ROE cases, since the starting point is the midpoint of the range of reasonableness, not the top of the range.

2. **Commission Determination**

12. We deny SoCal Edison’s request for rehearing on this issue, but we clarify our policy on proxy group composition. As discussed herein, we clarify that we will not mandate that a filing company must apply a regional proxy group in calculating its requested ROE.

13. In assessing whether a filing company’s proposed proxy group is appropriate, the Commission’s obligation is to ensure that the proposed proxy group consists of companies with comparable risks to those facing the applicant. While geographic proximity may be a relevant factor in identifying companies with comparable risks, it is not the sole basis for inclusion of companies in a proxy group. Thus, the Commission

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\[20\] SoCal Edison Rehearing Request at 29 (citing *Consumers Energy Co.*, 98 FERC ¶ 61,333 (2002)).
will not mandate that a proxy group must be composed of companies in the same geographic region as the filing company.

14. The question of which companies should be included in a proxy group is properly resolved based on the facts and circumstances of each case. In some cases, a filing company may rely solely on companies in its region to form a proxy group and to perform its DCF analysis, after demonstrating that these companies have comparable risk to the filing company. In other cases, a filing company may identify companies with comparable risk by looking beyond its geographic region. The filing company must, of course, fully support its choice of a proxy group, and intervenors are free to challenge the reasonableness of the filing company’s choice.

15. Here, the Commission did not mandate that Atlantic use a regional proxy group. Instead, Atlantic itself proposed using a WECC-wide proxy group rather than a national proxy group. Atlantic explained that it did not use companies operating only in CAISO, given the limited number of comparable companies. Instead, Atlantic’s expert “consider[ed] companies operating in the WECC region and the CAISO to be sufficiently comparable in terms of operating risks and transmission operations (all are members of the WECC).” As discussed above, Atlantic applied screening criteria that eliminated eight of the seventeen companies that were initially selected, leaving a final proxy group of nine companies that were located in the WECC. Atlantic applied a DCF analysis, the results of which are described in the testimony and work papers that were included as part of the December 2007 Filing. We reaffirm that Atlantic provided adequate support in its testimony and supporting materials for using a proxy group comprised of entities in the WECC.

16. Further, we note that SoCal Edison’s concern about using regional proxy groups was not squarely related to Atlantic Path 15’s use of such a proxy group, but rather about the broader policy issues that were raised by the February 2008 Order’s statements regarding the benefits of using a regional proxy group. Indeed, SoCal Edison does not object to the Commission’s summary approval of Atlantic’s proposed 13.5 percent ROE. As discussed above, we clarify that the Commission’s focus is on whether a proxy group includes companies of comparable business or financial risk, and we will not mandate that a proxy group must be composed of companies in the same geographic region as the filing company.

21 See December 2007 Filing, Ex. ATL-4 at 21-22.

22 Id., Ex. ATL-4 at 22.

23 See SoCal Edison Rehearing Request at 24.
17. Because we clarify our policy, as discussed herein, SoCal Edison’s alternative request for rehearing is moot and therefore denied.

B. **Up-Front ROE Determination**

1. **Rehearing Request**

18. SoCal Edison argues that the February 2008 Order provides a vehicle by which entities that want an up-front ROE determination can secure one without a trial-type evidentiary hearing. SoCal Edison contends that while regulatory certainty and prompt resolution may support the use of an up-front ROE determination approach in certain circumstances, such as in an incentive ROE case, mandating the use of such an approach for all ROE cases, particularly general rate cases, would be a major change in Commission policy and is inappropriate.\(^\text{24}\)

19. First, SoCal Edison explains that the considerations that may counsel for up-front ROE determinations in incentive rate cases (e.g., up-front decisions may help with financing projects) may not be present in general rate cases, which are more likely to be set for hearing for other issues. Second, SoCal Edison contends that a general rate case applicant that is willing to go to hearing should have the flexibility to develop a proxy group that is the most appropriate under the circumstances. Third, SoCal Edison argues that general rate cases require a more tailored analysis than incentive rate cases, because the focus in general rate cases is establishing a range of reasonable returns and placing the applicant’s ROE at an appropriate point in that range, while the focus in an incentive rate case is to ensure the applicant is not above the top of the range of reasonable returns. SoCal Edison asserts that this approach is consistent with Commission precedent.

2. **Commission Determination**

20. In response to SoCal Edison’s argument that we should not require an up-front ROE determination in all cases, we clarify that our decision to make an up-front ROE determination will depend on the facts and circumstances of each individual case.

21. While we note the February 2008 Order acknowledged that the use of regional proxy groups may allow for up-front ROE determinations, we recognize that choosing a regional proxy group is not independently dispositive. We will look at the facts and circumstances presented in each proceeding, including the written submissions of the

\(^{24}\) SoCal Edison Rehearing Request at 33-34 (citing *Southern Cal. Edison Co.*, 92 FERC ¶ 61,070, at 61,264 (2000)).
filing company and intervenors, in determining whether it is appropriate to make an up-front ROE determination or to order an evidentiary hearing.

22. Nonetheless, we affirm that the Commission retains discretion to make up-front ROE determinations if the record before it is sufficient to make such a summary finding. Recently, in *Pioneer Transmission LLC*, the Commission rejected the claim that it must always order trial-type hearings in ROE cases. As the Commission noted in *Pioneer*, federal courts have held that a formal trial-type hearing is unnecessary where there are no material facts in dispute. The Commission further emphasized that it is not sufficient for a protesting party merely to allege an issue of disputed fact—parties “must make an adequate proffer of evidence to support them.” The *Pioneer* order emphasized, “The Commission is only required to provide a trial-type hearing if the material facts in dispute cannot be resolved on the basis of written submissions in the record.”

23. The same principles that the Commission articulated in *Pioneer* may also be applied to general rate cases. If we are able to make summary determinations based on the written record, then we are not required to establish trial-type evidentiary hearing procedures. If intervenors believe that a trial-type hearing is more appropriate than an up-front ROE determination in general rate cases or incentive rate cases, we will consider such arguments on a case-by-case basis. Likewise, where filing companies themselves request that the Commission establish hearing procedures, we will consider those requests as well.

24. In light of this clarification with respect to the Commission’s approach to making up-front ROE determinations, we deny SoCal Edison’s alternative request for rehearing regarding that issue.

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25 130 FERC ¶ 61,044 (2010) (*Pioneer*).

26 *Id.* P 35 (citing *Moreau v. FERC*, 982 F.2d 556, 568 (D.C. Cir. 1993)). See also, e.g., *Blumenthal v. FERC*, 613 F.3d 1142, 1144 (D.C. Cir. 2010).

27 *Pioneer*, 130 FERC ¶ 61,044 at P 35 (quoting *Cerro Wire & Cable Co. v. FERC*, 677 F.2d 124, 129 (D.C. Cir. 1982)).

28 *Id.* n.73.
C. **Historical Test Year**

1. **Rehearing Request**

25. SoCal Edison argues that the Commission erred in approving Atlantic’s use of a historical test year in this proceeding and not setting the issue for hearing. In support, it states that because Atlantic’s rates are based on the cost of a single asset, the use of an historical test year in establishing Atlantic’s base TRR will overstate Atlantic’s costs, which will result in unjust and unreasonable rates. SoCal Edison explains that, unlike a traditional transmission service provider, Atlantic does not own a multi-component transmission system that needs to be improved through capital expenditures in order to meet the load demands of its customers. It asserts that, with the Commission’s summary approval of the use of a calendar year 2006 historical test period to support a TRR that becomes effective February 20, 2008, Atlantic will earn an actual ROE well in excess of the 13.5 percent, given that two years of accumulated depreciation are disregarded when the 2006 test year is used to calculate the base TRR. Thus, SoCal Edison contends that Atlantic should use a test year that reflects the period during which the rates will be in effect (i.e., 2008 or 2009); otherwise, Atlantic will receive an unjustified ROE windfall, which will increase as Atlantic’s cost-justified base TRR continues to decline as the company depreciates its plant.

26. SoCal Edison also argues that the Commission has previously ruled that the use of a historical test year for filing purposes does not preclude inquiry into whether the use of that test year is just and reasonable for purposes of setting rates. Specifically, SoCal Edison points to cases where it states the Commission recognized that even though the Commission’s regulations permit the use of historical test year information for filing purposes, using such a historical test year for a single asset company with a declining rate base for ratemaking purposes could result in unjust and unreasonable rates. It argues that the Commission’s decision to summarily approve the use of the historical test year disregards this precedent without explanation and is therefore arbitrary and capricious.

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29 SoCal Edison Rehearing Request at 12.

30 *Id.* at 13.

27. SoCal Edison also asserts that the Commission’s reliance upon a regulation that pertains only to section 205 filings to summarily dispose of the historical test year issue in the section 206 proceeding is error. In support, it states that none of the Commission’s regulations, including those promulgated under FPA section 205, prescribe the test year that may be used in a section 206 proceeding. SoCal Edison argues that even if the Commission properly relied upon section 35.13 in ruling upon Atlantic’s section 205 filing, those regulations have no bearing on the section 206 proceeding that the Commission commenced in the February 2008 Order. As a result, it argues that the Commission’s rationale for declining to set Atlantic’s use of a historical test year for hearing does not apply to the Commission’s section 206 proceeding.

2. Commission Determination

28. We will grant rehearing on this issue based on the circumstances presented here. We agree with SoCal Edison that Atlantic is not similarly situated to transmission providers with a number of different transmission assets of different vintages that could require new capital additions on a yearly basis. Atlantic is a new, single asset utility that has minimal probability for new transmission upgrades in the near term. Therefore, the underlying presumption that the use of an earlier time period historical test year, with plant balances that would have a significant time lag when compared to the effective date of the rates, may be just and reasonable because of the possibility of new intervening capital additions is not present in the instant proceeding. As the Commission has explained:

The ultimate purpose of a fully allocated cost of service filing before this Commission is to support a rate to be charged for the provision of electric service that is both fair and reasonable and which allows a utility to recover fully its cost of providing that service.... Synchronizing expenses, allocation factors, and billing determinants to the test period not only helps to ensure that each customer will pay its fair share of the costs incurred by the utility, but also helps to ensure that the utility’s revenues will match its costs.33

32 Id. at 20.

33 Delmarva Power and Light Co., 38 FERC ¶ 61,098, at 61,257 (1987), order denying reh’g, 43 FERC ¶ 61,250 (1988), aff’d mem. No. 88-1557 (D.C. Cir. 1989). See also, e.g., Westar Energy, Inc., 122 FERC ¶ 61,268, at P 98 (2008) (“Under Commission policy, companies must use a fully-synchronized test period cost-of-service study that uses either an historical test period or a projected test period.”)
29. Similarly, here we find that historical test year data, while adequate for suspension purposes, in certain situations may lead to an over-recovery of costs without appropriate adjustments. As such, our responsibilities under the FPA require that any potential over-recovery of costs be addressed and resolved. We also note that the parties to this proceeding have resolved through the uncontested Settlement all other pending cost-of-service issues (but for the two ROE issues being addressed in this order), so that we cannot ascertain whether other test year costs involving non-plant balances may have had significant changes. As such, based on the specific facts of this case, we will grant rehearing on this issue.

30. Section 3.3 of Settlement expressly contemplates Commission action on SoCal Edison’s request for rehearing. Specifically, this section provides that if the Commission or a court finds that the February 2008 Order was in error in approving Atlantic’s use of a historical test year and deciding not to set the issue for hearing, then Atlantic will reduce its Base TRR by $100,000 per year. Further, section 3.4 of the Settlement provides that within 30 days of the occurrence of a “Trigger Event” – which includes the issuance of this order granting rehearing on this issue – Atlantic shall file revised tariff sheets that reflect the applicable reduction in the base TRR.\(^34\) In accordance with sections 3.3 and 3.4 of the Settlement, we direct Atlantic to file revised tariff sheets reflecting the reduction of $100,000 in its base TRR within 30 days of the date of this order.

The Commission orders:

(A) SoCal Edison’s request for rehearing is granted in part and denied in part, as discussed in the body of this order.

\(^{34}\) Section 3.4 provides that Atlantic shall request an effective date for the revised tariff sheets that is the earlier of 60 days from the date of filing or 30 days prior to the effective date of a rate filing contemplated in section 5.1 of the Settlement. Section 5.1 states that Atlantic will file a revised base TRR by no later than February 18, 2011 with a requested effective date of April 19, 2011.
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(B) Atlantic is directed to submit a compliance filing within 30 days of the date of this order, as discussed in the body of this order.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,
Deputy Secretary.