

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

City of Azusa, California	Docket No. EL03-14-001
City of Anaheim, California	Docket No. EL03-15-001
City of Riverside, California	Docket No. EL03-20-001
City of Banning, California	Docket No. EL03-21-001
City of Vernon, California	Docket No. EL00-105-007
California Independent System Operator Corporation	Docket No. ER00-2019-007

ORDER DENYING REHEARING AND ESTABLISHING HEARING PROCEDURES

(Issued February 17, 2004)

1. On December 23, 2002, the Commission initiated settlement procedures in an order¹ responding to a remand from the United States Court of Appeals for the District of Columbia Circuit (Court)² concerning the Commission's review of the City of Vernon, California's (Vernon) Transmission Revenue Requirements (TRR). In addition, in an order issued concurrently with that Remand Order,³ the Commission consolidated the Vernon proceedings with proceedings filed by the City of Azusa, California (Azusa), the City of Anaheim, California (Anaheim), the City of Banning, California (Banning) and

¹ City of Vernon, California, et al., 101 FERC ¶ 61,353 (2002) (Remand Order).

² Pacific Gas and Electric Company v. FERC, 306 F.3d 1112 (D.C. Cir. 2002).

³ City of Azusa, California, et al., 101 FERC ¶ 61,352 (2002) (Consolidation Order).

the City of Riverside, California (Riverside) seeking a determination by the Commission that their TRRs are acceptable for the purpose of becoming Participating Transmission Owners (PTOs) in the California Independent System Operator Corporation (CAISO).

2. In this order, the Commission denies Vernon's rehearing request and establishes a hearing to ascertain whether Vernon's TRR results in a just and reasonable rate for the CAISO, and denies Vernon's request for rehearing of the Consolidation Order.

Background

3. On August 30, 2000, as supplemented on August 31, 2000, Vernon, a non-jurisdictional entity, filed a petition for declaratory order requesting a determination by the Commission that Vernon's TRR, as approved by its rate-setting body, the Vernon City Council, is proper for purposes of Vernon becoming a PTO in the CAISO. As a PTO, Vernon turns over operational control of its transmission entitlements to the CAISO and is reimbursed by the CAISO based upon its TRR and through the CAISO's collection of a transmission access charge (TAC) for transmission service provided to the CAISO's customers. In its request for a declaratory order, Vernon explained that its TRR uses proxy numbers for its rate of return and common equity and depreciation rates that are identical to those used by the IOU that is in the same TAC rate area, i.e., Southern California Edison Company (SCE). It further explained that it uses the same methodology for developing A&G expenses, cash working capital allowance and regulatory commission expense as used by SCE in its TRR proceeding. Vernon's proposed annual TRR is approximately \$13.1 million.

4. In an order issued on October 27, 2000,⁴ the Commission found that Vernon's proposed rate methodology and resulting high voltage TRR were just and reasonable, subject to certain modifications. In particular, while the Commission accepted Vernon's use of SCE's return on common equity (11.6 percent), the Commission required Vernon to use SCE's capital structure. The Commission also required Vernon to remove from its TRR the inclusion of unused transmission capacity expense as inconsistent with the costs that SCE includes in its TRR. The Commission denied rehearing of this order.⁵

⁴ City of Vernon, California, 93 FERC ¶ 61,103 (2000) (October 2000 order), order on reh'g, California Independent System Operator Corporation, et al., 94 FERC ¶ 61,148 (2001), remanded, Pacific Gas and Electric Company v. FERC, 306 F.3d 1112 (D.C. Cir. 2002), order on remand, City of Vernon, California, et al., 101 FERC ¶ 61,353 (2002) (Remand Order).

⁵ California Independent System Operator Corporation, et al., 94 FERC ¶ 61,148 (2001) (February 2001 Order).

5. Pacific Gas and Electric Company (PG&E) appealed the Commission's October 2000 and February 2001 orders to the Court. On October 15, 2002, the Court remanded to the Commission the question of whether the review conducted by the Commission of the revenue requirements of a non-jurisdictional entity – Vernon – that is a part of a jurisdictional Independent System Operator (ISO) – the CAISO – was sufficient to ensure that the CAISO's rates will be just and reasonable under Section 205 of the Federal Power Act (FPA).⁶

Court Ruling

6. The Court rejected PG&E's argument that Vernon's TRR must be independently subjected to the just and reasonable standard of Section 205 of the FPA. It explained that the Commission may use a different approach so long as the Commission can ensure by examining Vernon's TRR that the CAISO's rates will be just and reasonable.

7. The Court then explained that while there was no objection to the general approach taken by the Commission, it was unclear under what standard the Commission reviewed Vernon's TRR to ensure that a pass through of its costs by the CAISO would be just and reasonable. It further pointed out that, in contrast, the Commission elsewhere asserted that the purpose of its review was to determine whether Vernon's rate methodology will result in a just and reasonable component of CAISO's rates. The Court concluded that the Commission never clarified and developed either the approach or the standard that it applied in this case.

8. The Court added that the Commission did not claim that its standards ensure that Vernon's TRR itself will be just and reasonable, but noted that the Commission's approach might be acceptable if the Commission tested the final CAISO composite rate to determine whether it was just and reasonable (which it noted the Commission had not done). Consequently, the court remanded the case so that the Commission could articulate with clarity the approach and standard it would use that would ensure that CAISO's rates are just and reasonable under Section 205 of the FPA.

Other procedural and substantive matters

9. The Court stated that on remand the Commission must be able to show that there was substantial evidence to support a conclusion that the CAISO's rates after the inclusion of Vernon's TRR are just and reasonable.

10. In reviewing Vernon's costs, the Court explained that the Commission does not need to apply to non-jurisdictional utilities its regulations that are applicable to

⁶ Pacific Gas and Electric Company v. FERC, 306 F.3d 1112 (D.C. Cir. 2002).

jurisdictional utilities. It concluded that the Commission's review of Vernon's costs was not arbitrary and capricious, but again explained that the problem is the amorphous standard by which the Commission reviewed the impact of Vernon's TRR on CAISO's rates.

11. With respect to Vernon's use of SCE as a proxy for the rate of return on common equity and the depreciation rate, the Court found that the Commission provided only an inadequate conclusory statement that the Commission thought use of the proxy was appropriate because SCE and Vernon were in the same TAC area. The Court noted that Vernon itself sought to distinguish itself from SCE and that the Commission had left unanswered protests to the use of SCE's rates. The Court further explained that on appeal, the Commission maintained that it was necessary for Vernon to rely on SCE's capital structure and overall return as a proxy because Vernon's return could only be measured indirectly, and Vernon and SCE had the same risks because they provide services in the same TAC area. However, the Court noted, the Commission's orders on review did not provide that explanation and the Court could not rely on the Commission's post hoc justifications for its action.

Commission Orders

12. In the Remand Order, the Commission responded to the Court's remand and initiated settlement procedures for the parties to resolve the matters at issue concerning Vernon's TRR.

13. On October 18, 2002, the City of Azusa, California (Azusa) and the City of Anaheim, California (Anaheim) filed petitions for a declaratory order requesting a determination by the Commission that their respective Transmission Revenue Requirement (TRR), as approved by their respective rate-setting body, is acceptable for the purpose of becoming Participating Transmission Owners (PTOs) in the CAISO. On October 29, 2002, the City of Riverside, California (Riverside) and the City of Banning, California (Banning) filed similar petitions requesting the same relief.

14. In the Consolidation Order, the Commission found that these four dockets raised similar issues and also raised issues similar to those being addressed in the Remand Order. Accordingly, we initiated settlement proceedings with respect to the four petitions filed by Azusa, Anaheim, Riverside and Banning, and also consolidated those proceedings with the Vernon proceeding in the Remand Order.

Vernon's Request for Rehearing

15. On January 22, 2003, Vernon filed a request for rehearing and clarification of the Remand Order and the Consolidation Order. Vernon contends that the Court expressed concern over only two aspects of the Commission's review of Vernon's TRR – rate of

return and the depreciation rate. Vernon states that the Court found that the basis for the Commission's application to Vernon of the percentages used by SCE to set its rates was inadequately explained in the underlying Commission's orders on review. Vernon requests that the Commission provide the further explanation of its approval of Vernon's Transmission Revenue Requirement as directed by the Court, instead of, or at least prior to, establishing any further proceedings, including settlement procedures. In addition, Vernon requests that the Commission reverse the decision to consolidate the Vernon proceedings with the proceedings involving the Azusa, Anaheim, Riverside and Banning October 2002 petitions for a declaratory order on their TRRs.

16. On February 6, 2003, SCE, SDG&E and PG&E (collectively, the Original Participating Transmission Owners (OPTOs) filed a joint response to Vernon's request for Rehearing and Clarification.

17. On April 28, 2003, the Public Utilities Commission of the State of California (California Commission) filed a motion for leave to intervene out of time. California Commission is a party to the consolidated proceeding having previously intervened in the Vernon proceeding in Docket No. EL00-105-000. However, California Commission now seeks to intervene with respect to issues that have arisen regarding the impact on CAISO rates of the Anaheim and Riverside TRR proposals and states that it now moves, out of an abundance of caution, to intervene out of time so that it can continue to be a party in the Anaheim and Riverside dockets should the Vernon case be severed.

Discussion

Procedural Matters

18. We will dismiss the California Commission's motion to intervene as unnecessary. By virtue of the consolidation of the proceedings, California Commission's intervention in Docket No. EL00-105-000, one of the consolidated proceedings, made it a party to each of the consolidated proceedings. Thus, no further action is needed by California Commission to participate in the particular proceedings concerning the Anaheim and Riverside TRR proposals, whether or not they ultimately are severed from these consolidated proceedings.

19. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 213(a)(2) (2003), prohibits an answer to a rehearing request unless otherwise ordered by the decisional authority. We are not persuaded to accept OPTO's answer and will, therefore, reject it.

Analysis

20. The Commission denies Vernon's rehearing request that the Commission provide further explanation of its review of Vernon's TRR instead of, or at least prior to, establishing further proceedings. Initially, in response to the Court's remand, the Commission initiated settlement procedures for the parties to resolve the matters at issue. Those settlement procedures were unsuccessful with respect to Vernon.⁷ Thus, in light of the Court's finding that the Commission had not shown that Vernon's TRR would result in just and reasonable CAISO rates, we will establish hearing procedures to explore the appropriate TRR for Vernon that will ensure that the CAISO's rates after the inclusion of Vernon's TRR are just and reasonable. The Commission will not set for hearing just Vernon's rate of return and depreciation rate because it must determine that Vernon's overall TRR, comprised of all of its rate components, when included in the CAISO's rates result in just and reasonable CAISO rates.

21. We direct the Chief Administrative Law Judge or his designee to appoint a presiding judge to convene a conference no later than fifteen days from the date of this order.

Consolidation Order

22. On May 20, 2003, the Chief Administrative Law Judge temporarily suspended the settlement proceedings with respect to Vernon until such time as the Commission issues an order on the merits of Vernon's rehearing request. The Chief Judge indicated that this was done so that settlement proceedings could continue among Azusa, Anaheim, Riverside and Banning. On July 18, 2003, Azusa, Anaheim, Riverside and Banning filed an Offer of Settlement and Settlement Agreement (Settlement) that resolved all issues concerning the TRRs for the Cities of Azusa and Banning. The Settlement Agreement also conditionally resolves all issues concerning the TRRs for the Cities of Anaheim and Riverside, subject to the establishment of evidentiary hearing procedures to address and resolve certain outstanding issues. In an order issued on December 18, 2003,⁸ the Commission accepted the uncontested Settlement for filing and established an evidentiary hearing to resolve the outstanding issues concerning Anaheim's and Riverside's TRRs. In light of these actions, the Commission will deny Vernon's request for rehearing of the Consolidation Order, but without prejudice to the Chief Administrative Law Judge determining what procedures are best suited to resolve these matters, including whether to sever one or more of these dockets from another.⁹

⁷ See *infra* P 22.

⁸ *City of Azusa, California, et al.*, 105 FERC ¶ 61,293 (2003).

⁹ See 18 C.F.R. § 385.503 (a)(2003).

The Commission orders:

(A) Vernon's request for rehearing is denied, as discussed in the body of this order.

(B) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Federal Energy Regulatory Commission by Section 402(a) of the Department of Energy Organization Act and the Federal Power Act and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the Federal Power Act (18 C.F.R., Chapter 1), a public hearing shall be held to resolve the outstanding issues, as discussed in the body of this order.

(C) A Presiding Administrative Law Judge, to be designated by the Chief Administrative Law Judge, shall convene a prehearing conference in the proceeding, to be held within approximately 15 days of the designation of the presiding judge in a hearing room of the Federal Energy Regulatory Commission, 888 First St., N.E., Washington, D.C. Such conference shall be held for the purpose of establishing a procedural schedule. The presiding judge is authorized to establish procedural dates and to rule on all motions (except motions to dismiss), as provided in the Commission's Rules of Practice and Procedure.

By the Commission.

(S E A L)

Linda Mitry,
Acting Secretary.