

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Midwest Independent Transmission System
Operator, Inc.

Docket Nos. ER02-2458-000
ER02-2458-001

ORDER CONDITIONALLY APPROVING SETTLEMENT

(Issued March 5, 2004)

Introduction

1. In this order we conditionally approve an offer of settlement that establishes a new joint pricing zone under the Midwest Independent Transmission System Operator, Inc.'s (Midwest ISO) open access transmission tariff (OATT). The action in this order benefits customers because it facilitates a fair and reasonable solution to matters affecting rates for service.

Background

Commission Order

2. In August 2002, the Midwest ISO submitted proposed revisions to Schedules 7, 8, and 9 of the Midwest ISO OATT designed to create a separate pricing zone for Wolverine Power Supply Cooperative, Inc., (Wolverine). Midwest ISO based the proposed revisions on a version of Section II.A.1 of Appendix C of the Midwest ISO Agreement that permits the creation of a new pricing zone under certain conditions. Midwest ISO argued that Wolverine was entitled to a separate pricing zone because it was a transmission provider under the Wolverine OATT and Wolverine operates a fully integrated transmission system connected with, and electrically surrounded by, the transmission system currently owned by Michigan Electric Transmission Company LLC (METC). Midwest ISO maintained, therefore, that Wolverine was in compliance with the requirements set forth in Section II.A.1.

3. The Commission rejected, without prejudice, the proposed Wolverine pricing zone. The Commission determined that Wolverine did not meet the standard set out in Section II.A.1¹ that was in effect or the standard set out in the proposed revised Section II pending in another docket.²

4. However, the Commission concluded that the parties had raised important issues that must be addressed in order to further the development of the Regional Transmission Organization (RTO). The Commission pointed out that the participation of new transmission owners should be encouraged by providing appropriate compensation for their transmission facilities, whether by establishing separate pricing zones for those entities or by incorporating those entities into existing pricing zones. The Commission noted that Section III.A.8 of Appendix C to the Midwest ISO Agreement set out the mechanism whereby multiple owners in a zone could agree to the equitable distribution of zonal revenues.

5. The Commission established settlement judge procedures so that the parties could develop a joint METC/Wolverine pricing zone that accommodates Wolverine's participation in Midwest ISO and compensates Wolverine for its transmission facilities.³

¹ Section II.A.1 of Appendix C of the Midwest ISO Agreement that was in effect when Midwest ISO filed the proposed revisions stated in pertinent part:

[The Zones] only may be changed to reflect the effectuation of a merger . . . , to add a new Owner that operates a control area in existence on or before the date of the initial filing with the FERC to establish the Midwest ISO, or to reflect the withdrawal from the Midwest ISO of an Owner or Owners.

² The proposed revised Section II permits Midwest ISO to create a pricing zone when it adds "a new Owner that is an existing transmission provider and is or would have been a specified zone for pricing under an existing or proposed regional transmission tariff." This proposed revised Section II was subsequently accepted for filing in Midwest Independent Transmission System Operator, Inc., 101 FERC ¶ 61,113 (2002).

³ The Commission set out the parameters of the settlement proceedings by stating:

We agree with the protesters that Wolverine's transmission facilities must meet the requirements of the seven factor test, as interpreted by the Michigan Commission, [footnote omitted] in order to ensure that Wolverine receives compensation for its transmission facilities on a basis comparable to the compensation received by [METC]. Application of the seven factor test

(continued...)

Proposed Settlement Agreement

6. Midwest ISO, Wolverine, Michigan Public Power Agency (MPPA), METC, International Transmission Company (ITC), Dairyland Power Cooperative (Dairyland), Trans-Elect, Inc. (Trans-Elect), Commission Trial Staff (Trial Staff), and Consumers Energy Company (Consumers) participated in the settlement proceeding established in Midwest ISO-Wolverine. During that proceeding, the Chief Judge denied Michigan Public Service Commission's (Michigan Commission) late motion to intervene filed after Midwest ISO-Wolverine was issued. The Chief Judge found that to permit the Michigan Commission's late intervention would result in delay, disruption, and place an undue burden on the negotiating parties.

7. On July 11, 2002, Midwest ISO, MPPA, METC, and Wolverine (collectively, Filing Parties) filed an Offer of Settlement intended to settle and resolve all issues pending in this docket.⁴ The Offer of Settlement includes, among other things, a Proposed Settlement Agreement and related Revenue Allocation Agreement (RAA) between the executing parties.⁵ The Offer of Settlement proposes to establish a joint pricing zone within Midwest ISO that will include Wolverine, METC and MPPA.⁶

(...continued)

should form the starting point for these negotiations. In order to aid the parties in this process, we will establish settlement judge procedures to address, among other things, revenue allocation among RTO members within the [METC] pricing zone.

See Midwest Independent Transmission System Operator, Inc., 101 FERC ¶ 61,004 at P 21 (2003), reh'g pending (Midwest ISO-Wolverine).

⁴ According to the Filing Parties, if the Commission accepts the Offer of Settlement without alteration, Wolverine's pending request for rehearing will be withdrawn.

⁵ Midwest ISO, METC, MPPA, and Wolverine are parties to the proposed Settlement Agreement. METC, MPPA, and Wolverine are the only parties to the RAA.

⁶ The Proposed Settlement Agreement also sets out the criteria for others to join this joint pricing zone.

8. Dairyland, Trial Staff, MPPA, METC, and ITC filed comments generally supporting the Offer of Settlement. Consumers filed comments opposing the Offer of Settlement.

9. The Michigan Commission renewed its motion to intervene out of time. Wolverine filed an answer opposing the late motion to intervene. Consumers filed an answer that supported the late motion to intervene and responded to some portions of the Wolverine answer.

10. The Michigan Commission also filed comments opposing the Offer of Settlement and a motion to lodge its Administrative Determination of August 26, 2003 (August 26 Order). The Michigan Commission's August 26 Order characterized Wolverine's facilities using the seven factor test. Wolverine filed an answer opposing the motion to lodge. Consumers filed an answer supporting the motion to lodge and addressing some portions of the Wolverine answer.

11. The settlement judge filed a report of the contested Offer of Settlement on August 14, 2003. The settlement judge listed several contested issues including, but not limited to, the makeup of a joint pricing zone that would include METC, Wolverine, MPPA, and possibly others (Joint Zone); the treatment of lost revenues and trapped costs during the rate freeze in Michigan; and the role of the seven factor test in determining which facilities are to be included in the Joint Zone.⁷

12. The motions, comments, and responses are discussed in detail below.

Discussion

Procedural Matters

13. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §385.214 (2003), we will deny the Michigan Commission's motion to intervene because it has failed to demonstrate good cause warranting the grant of late intervention. Parties seeking late intervention where the proceedings are advanced bear a heavy burden to demonstrate good cause for the granting of such late intervention because the prejudice

⁷ See *Midwest Independent Transmission System, Inc.*, 104 FERC ¶ 63,038 at P 5 (2003) (Settlement Judge Report). The Chief Judge terminated the settlement judge procedures on August 21, 2003.

to other parties may be substantial.⁸ We believe that the prejudice to the parties involved in the settlement negotiations would be substantial if the Michigan Commission were permitted to intervene at this late date. We find that the Michigan Commission has not alleged any facts explaining its late motion to intervene that would meet this heavy burden.

14. However, we will grant the Michigan Commission's motion to lodge its August 26 Order. We find that the August 26 Order is relevant and facilitates our analysis of the Offer of Settlement.

Substantive Matters

Ownership Entitlements⁹

15. The Proposed Settlement Agreement recognizes transmission ownership and operating agreements that outline Wolverine's, MPPA's, and METC's joint ownership of certain transmission facilities on the METC system.¹⁰ Control of these jointly-owned facilities and all of METC's facilities have already been transferred to Midwest ISO.¹¹ However, METC does not include the cost of Wolverine's or MPPA's ownership shares in its revenue requirement and neither Wolverine nor MPPA recover any costs related to their ownership shares in the jointly-owned facilities from Midwest ISO.

16. In exchange for Wolverine's and MPPA's continued payment for costs related to their ownership shares, Wolverine and MPPA receive transmission service rights on

⁸ We note that the Michigan Commission first filed a late motion to intervene after settlement judge procedures were implemented and this motion was denied by the Chief Judge because it would result in "unjustified delay, disruption of the settlement proceedings, and place an undue burden on the negotiating parties." Settlement negotiations took place over nine months, without the Michigan Commission's participation. The Michigan Commission's late motion to intervene is not justified given the late stage of this proceeding (*i.e.* the parties reached a settlement and the settlement proceedings were terminated).

⁹ The proposed Offer of Settlement describes ownership entitlements as 120.98 MW of transmission service for Wolverine and approximately 366.5 MW for MPPA, subject to adjustment. See Offer of Settlement, Article II and Sections 4.2 and 4.3.

¹⁰ These ownership and operating agreements are listed as Grandfathered Agreements under the Midwest ISO OATT.

¹¹ See Trans-Elect, Inc., 99 FERC ¶ 61,068 (2002).

METC's system. Midwest ISO then offsets Wolverine's and MPPA's network load by the amount of their transmission service rights. Consequently, Wolverine and MPPA only pay Midwest ISO for the amount of transmission service above and beyond their transmission service rights on the METC system. In the Proposed Settlement Agreement, the Filing Parties seek to continue this arrangement (*i.e.* Wolverine and MPPA will continue to pay all costs associated with their ownership shares in the jointly-owned facilities and will not recover these costs under any Midwest ISO OATT revenue requirement).

17. Consumers argues that the proposed transmission service rights for Wolverine and MPPA's ownership shares are not consistent with Order No. 2000's requirement that an RTO be the only provider of transmission service over the facilities under its control and that the RTO must be the sole administrator of its own Commission-approved OATT.¹² In addition, Consumers asserts that the Proposed Settlement Agreement does not provide for Wolverine and MPPA to pay charges or costs associated with the use of Wolverine and MPPA facilities in connection with the capacity rights under the Grandfathered Agreements.¹³ Consumers objects to the continued offset to Wolverine's and MPPA's network load for the transmission service rights under the ownership and operating agreements after the joint zone rate is implemented. This offset, Consumers argues, would result in Wolverine and MPPA paying nothing for their use of the Wolverine and MPPA facilities included in the joint zone to serve this deducted load.

18. Wolverine and MPPA answer Consumers' assertions by pointing out that treatment of the ownership entitlements has not changed and is the same arrangement that was in place when Consumers owned the METC transmission facilities. The Proposed Settlement Agreement simply maintains the status quo. Wolverine and MPPA also state

¹² See Regional Transmission Organizations, Order No. 2000, 65 Fed. Reg. 809 (January 6, 2000), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,089 at 31,200-31,201 (1999), order on reh'g, Order No. 2000-A, 65 Fed. Reg. 12,088 (March 8, 2000), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,092 (2000), aff'd sub nom. Public Utility District No. 1 of Snohomish County Washington, et al. v. FERC, 272 F.3d 607 (D.C. Cir. 2001).

¹³ Consumers argues that Wolverine and MPPA should be responsible for these costs because the proposed Settlement Agreement backs out their use of the transmission entitlements based on ownership in METC facilities making the deducted load that is directly connected to Wolverine's and MPPA's facilities exempt from any cost responsibility for those facilities while Consumer's load (which is not directly connected to them) would be assessed over ninety six percent of those costs.

that Midwest ISO is the sole provider of transmission service over the jointly-owned facilities and has been since METC transferred control of its facilities to Midwest ISO.

Commission Determination

19. We find the continued use of transmission service rights pursuant to Grandfathered Agreements already under the Midwest ISO OATT is just and reasonable. The jointly-owned facilities in question are and will continue to be under the sole control of Midwest ISO and all transmission service over these facilities will be under the Midwest ISO OATT.¹⁴ As before, Wolverine's and MPPA's costs related to the jointly-owned facilities will not be included in any transmission revenue requirement recovered under the Midwest ISO OATT.¹⁵ Wolverine and MPPA will also continue to pay Midwest ISO for the transmission service that is over and above the transmission service rights they receive under the Grandfathered Agreements. However, as Consumers points out, under the Proposed Settlement Agreement, Wolverine and MPPA would not be responsible for the cost of their own facilities used to serve the load associated with the transmission service rights. The Grandfathered Agreements provide for transmission service over the METC transmission system, not for transmission service over the Wolverine and MPPA facilities, used to transmit power to Wolverine's and MPPA's members. In order to ensure that Wolverine and MPPA bear the appropriate share of the cost of their facilities used to deliver power wheeled under the Grandfathered Agreements once the Joint Zone is implemented, Wolverine and MPPA must exclude from their transmission revenue requirements recovered through the Joint Zone rate, a pro rata share (i.e., load associated with the transmission service rights as a proportion of total Joint Zone load excluding such transmission service rights) of the total revenue requirements associated with their facilities included in the Joint Zone.

¹⁴ We disagree with Consumers' contention that the treatment of the transmission service rights violates the Order No. 2000 requirement that an RTO be the sole provider of transmission service over the facilities under its control. Section 37.34 of the Midwest ISO OATT specifically provides that "transmission owning members will have to take transmission service under the Midwest ISO (OATT) for their use of the Midwest ISO transmission system to serve bundled load and grandfathered agreement customers."

¹⁵ However, costs for METC's share of jointly owned facilities will be included in the rates.

Double Recovery

20. According to Consumers, Wolverine will double collect its transmission charges: once through its existing bundled wholesale rates and once through the proposed Midwest ISO OATT charges. Wolverine and MPPA challenge Consumers' double collection assertion. They point out that the costs associated with the jointly-owned facilities will not be included or recovered under the Midwest ISO OATT and, thus, there will be no double recovery of those costs. In addition, Wolverine commits to revising its bundled wholesale agreements to account for any change in revenues resulting from the transfer of its facilities to the control of Midwest ISO.

Commission Determination

21. We agree with Wolverine and MPPA that there will be no double recovery for the cost of the jointly-owned facilities because their costs associated with the jointly owned facilities will not be included in their revenue requirement under the Midwest ISO tariff. Furthermore, we accept Wolverine's commitment to revise its exiting wholesale rates to reflect any changes in its revenues resulting from its participation as a transmission owning member of Midwest ISO and which result in lower costs to customers paying such rates. Wolverine must file such revisions with the Commission within 30 days of the effective date of the Proposed Settlement Agreement.

Mobile-Sierra Language

22. Trial Staff expresses concern that certain language in the Proposed Settlement Agreement binds the Commission to the "public interest" standard of review for all changes to the Proposed Settlement Agreement. Trial Staff asserts that in prior cases, the Commission has stated that a restriction on its authority to order changes to an agreement, like that in the Proposed Settlement Agreement, affects its ability under the Federal Power Act to protect the public interest – particularly the interest of non-parties to an agreement.

23. Wolverine responds to Trial Staff's concern stating that the Proposed Settlement Agreement is not intended to bind the Commission acting sua sponte or in response to a complaint filed by a third party. According to Wolverine, the Filing Parties agree to amend the last sentence of Section 8.4 of the Proposed Settlement Agreement to read as follows:

The standard of review for any changes proposed by the Executing Parties other than those expressly provided for herein shall be in the "public interest" standard of review...

Commission Determination

24. We agree that the proposed revision clarifies that the imposed standard of Commission review applies only to proposed changes that are filed by signatories to the settlement agreement. Thus, Commission may, either sua sponte or pursuant to a complaint by a non-party to the settlement, in order to protect the interests of non-parties, investigate rates, terms and conditions under a "just and reasonable" standard at such times and under such circumstances as it deems appropriate.¹⁶

Losses

25. The Proposed Settlement Agreement at section 6.9 states that the Greater Michigan Joint Zone, that includes METC, Wolverine and MPPA, shall serve as a single loss zone and that the Filing Parties shall continue to work in good faith and will submit an amendment to the Proposed Settlement Agreement that addresses the requirements for a single loss zone as soon as practicable. Consumers argues that the Commission should summarily reject the proposal to combine the METC, Wolverine and MPPA facilities into a single loss zone with METC because, among other things, the details of the single loss zone methodology are not explained.

Commission Determination

26. We believe the proposal for a single loss zone in the Joint Zone is appropriate. A simplified, uniform single loss rate across the Joint Zone is consistent with Attachment M to the Midwest ISO OATT, which stipulates loss zones that conform to the boundaries of either control areas or pricing zones.¹⁷ Consumers has not justified departure from this current Midwest ISO practice. However, as Consumers points out, we do not have the details of the single loss zone proposal. We therefore direct Wolverine to revise section 6.9 to provide a detailed description of the loss zone methodology within thirty days of the date of this order.

¹⁶ See, e.g., PJM Interconnection, LLC, 96 FERC ¶ 61,206 at n13 (2001); Turlock Irrigation District and Pacific Gas and Electric Company, 88 FERC ¶ 61,322 (1999), citing Carolina Power & Light Company, 67 FERC ¶ 61,074 (1994). Accord, Cities of Anaheim, et al. v. Deseret Generation & Transmission Co-operative, 90 FERC ¶ 61,236 at 61,755 (2000).

¹⁷ See e.g., Midwest Independent System Operator, Inc., 103 FERC ¶ 61,028 (2002).

Rate of Return on Equity

27. Wolverine and MPPA propose to use a 12.88 percent rate of return on equity (ROE) when calculating their rates pursuant to Attachment O of the Midwest ISO OATT. Wolverine asserts that the 12.88 percent ROE is consistent with the Commission's order that permitted a single ROE component to be used by participating Midwest ISO transmission owners in Attachment O to the Midwest ISO OATT.¹⁸ Wolverine also states that once functional control of its transmission facilities is turned over to Midwest ISO and Wolverine and MPPA become participating Midwest ISO transmission owners, they are entitled to that 12.88 percent ROE.¹⁹

28. Consumers asserts, without elaboration, that a 12.88 percent ROE may not be appropriate for Wolverine and MPPA.²⁰

29. Trial Staff states that while the Commission approved the 12.88 percent ROE for all participating transmission owners, it is unclear whether the Commission intended for cooperatives and municipals to also receive that 12.88 percent ROE. Trial Staff also states that this determination is a policy call for the Commission. Trial Staff takes no position as to the appropriate ROE for Midwest ISO members who are cooperatives and municipals.²¹

Commission Determination

30. The Commission established the 12.88 percent ROE in a proceeding where a group of Midwest ISO transmission owners, including several public power participants, proposed an ROE that would apply to all pricing zones under the Midwest ISO OATT except the American Transmission Company zone. We find that the 12.88 percent ROE approved in that proceeding applies to the transmission rates for all transmission owners under Attachment O of the Midwest ISO OATT, unless those transmission owners have received approval for a different ROE.²²

¹⁸ Midwest Independent Transmission System Operator, Inc., 100 FERC 61,292 (2002), reh'g denied, 102 FERC 61,148 (2003).

¹⁹ Explanatory Statement at 34.

²⁰ Consumers Comments at 45.

²¹ Trial Staff Comments at 18-19.

²² Midwest Independent Transmission System Operator, Inc., 100 FERC 61,292 (2002), reh'g denied, 102 FERC 61,148 (2003).

31. Consistent with our policy outlined in Order No. 2000, we continue to encourage participation of all transmission owners in RTOs, including cooperatives and municipals. Their participation will enhance the reliability and economic benefit of RTOs and ensure appropriate RTO size and scope. It is unlikely that Wolverine or any other small transmission owner will participate in an RTO without proper and equitable compensation for their transmission facilities. We find that once Wolverine and MPPA become participating members of Midwest ISO by turning over control of their transmission facilities to Midwest ISO, they should receive the same 12.88 percent ROE afforded to other transmission owners in Midwest ISO.

Deferral Amounts

32. Customers in the METC pricing zone are paying a rate that is currently frozen until December 31, 2004 (Capped Rate). The Filing Parties propose a two-stage rate for the Joint Zone. Stage 1 begins on the date that Wolverine and MPPA transfer their facilities to Midwest ISO and continues through December 31, 2005. During Stage 1, the customers within the Joint Zone will continue to pay the current Capped Rate. However, during Stage 1, a "Theoretical Rate" will also be calculated for the purpose of creating Deferred Revenue Accounts. The Theoretical Rate is the sum of the METC rate component, which is equal to the Capped Rate, plus the rate components for the other Joint Zone Transmission owners (*i.e.*, the amount that would have been charged to meet the other Joint Zone transmission owners' revenue requirements for their transmission facilities, absent the rate cap). The difference between the Capped Rate and the Theoretical Rate is recorded and multiplied by the usage of the Joint Zone transmission system, which is recorded in a Deferred Revenue Account that will be established for each Joint Zone transmission owner.

33. Stage 2 begins on January 1, 2006, and ends on January 31, 2008 (concurrent with the end of the Midwest ISO transition period). During Stage 2, the rate for transmission service in the Joint Zone will be set at the sum of the applicable rate components for all of the Joint Zone transmission owners, as adjusted for the recovery of previously deferred amounts recorded in the Deferred Revenue Account, any performance-based rate component, and any other authorized deferrals. The Deferred Revenue Account recovery component for each Joint Zone transmission owner, including any carrying charges, will be amortized and recovered monthly during Stage 2. Half of the deferred amounts will be amortized and recovered in 2006 and the other half of the deferrals will be amortized and recovered in 2007, with a "true-up" period for any under-or-over-recoveries in January 2008.

34. Consumers asserts that the deferral mechanism is simply a cloaked way of charging more than the Capped Rate and collecting that excess at a later date. Consumers argues

that the deferral mechanism is contrary to the moratorium currently in place on changes to transmission rates paid by wholesale customers in the METC pricing zone.

35. Trial Staff supports creation of the Joint Zone and the two-stage rate structure proposed for rate development and revenue distribution. Trial Staff points out that the two-stage rate structure leaves the rate freeze in place until the end of 2005, and allows the other Joint Zone transmission owners to recover the costs of their transmission facilities. Trial Staff argues that the terms of the settlement will minimize cost impacts while allowing other positive aspects of the Joint Zone, including coordinated planning and integrated operations of a larger transmission network, to go forward immediately.

36. Wolverine argues that bringing in new facilities to an RTO adds costs to the RTO revenue requirements that should be allocated to RTO customers. Wolverine also argues that even if some RTO customers incur increased costs, that does not mean that the cost allocation is, as Consumers argues, an illegitimate revenue enhancement. Wolverine asserts that a transition mechanism, such as the rate cap and deferral mechanism contained in the Proposed Settlement Agreement, is appropriate to minimize cost shifts.

37. METC states that it will not benefit financially from the creation of the Joint Zone and that it cannot afford to subsidize the costs of the Joint Zone. According to METC, the proposed deferral mechanism is necessary for it to recover costs during the rate freeze and to ensure that it is not harmed by the formation of the Joint Zone.

Commission Determination

38. We will accept the proposed deferral mechanism. The METC pricing zone's current rates were approved when Consumers transferred its transmission facilities to METC.²³ The current rates include a rate moratorium through December 31, 2004, and deferred recovery of the costs of new transmission facilities placed into service during the moratorium. The proposed deferral mechanism submitted in the Offer of Settlement is similar to the one approved in Trans-Elect in that it provides near term rate certainty in the Joint Zone and ensures that members of the Joint Zone will recover the costs in a just and reasonable manner. We find that the deferral mechanism proposed in the instant case also furthers the goals of Order 2000 because it facilitates the participation of additional transmission-owning members in Midwest ISO and allows them the opportunity to receive compensation for their transmission facilities on a comparable basis to that received by METC.

²³ Trans-Elect, Inc. et al., 98 FERC ¶ 61,142 (2002), order on reh'g, 98 FERC ¶ 61,368 (2002) (Trans-Elect).

39. Therefore, we will approve the two-stage rate proposal for the Joint Zone, including the use of the deferral mechanism through December 31, 2005, the end of the rate moratorium. Our acceptance of the proposal in the Settlement Agreement extends the moratorium for rates in the METC pricing zone, and also freezes the METC component of the Joint Zone rate, by one year beyond that approved in Trans-Elect (i.e. December 31, 2004). In granting this approval, we recognize that the moratorium and deferral mechanism are parts of an entire settlement package resolving numerous issues associated with the creation of the Joint Zone.

Carrying Charge on Deferral Amounts

40. The Proposed Settlement Agreement includes a proposed carrying charge applicable to the amounts placed in the deferral accounts described above. Article II of the Proposed Settlement Agreement provides that the carrying charge will be the "return calculated pursuant to Attachment O of the Midwest ISO OATT." The Explanatory Statement, however, states that the carrying charge for the deferrals is 12.88 percent, the ROE approved for use by the Midwest ISO transmission owners under the transmission formula rate in Attachment O to the Midwest ISO OATT. The Explanation Statement states that the carrying charge is designed to compensate parties for the time value of money and that the charge is a marginal opportunity cost that should equal the higher of the cost of a party's worst debt or the return available on its best available investment.

41. Consumers asserts that the proper carrying charge rate for any rate collections deferred from Stage 1 to Stage 2 is the refund interest rate established in Section 35.19 of the Commission's regulations (18 C.F.R. § 35.19 (2003)).

42. Trial Staff argues that the Filing Parties have not supported using the ROE for the carrying charge on the deferred amounts. Instead, Trial Staff proposes the overall rate of return from the Midwest ISO OATT Attachment O rate formula as the carrying charge for deferrals.

43. Wolverine states that in the Explanatory Statement, the Filing Parties inadvertently proposed to use the 12.88 percent ROE, approved for transmission owners within Midwest ISO, as the carrying charge. Wolverine confirms that the parties to the Proposed Settlement Agreement propose to use the overall rate of return from the Midwest ISO OATT Attachment O rate formula as the carrying charge on deferrals. Wolverine also states that this proposal is preferable to the less predictable and more complex standard refund interest rate.²⁴

²⁴Wolverine Reply Comments at 26.

44. METC supports using the overall rate of return as a carrying charge because it is more predictable and less complex than the Commission's standard refund interest rate. In addition, METC asks that the Commission confirm that the rate of return applicable to its deferral mechanisms approved in Trans-Elect²⁵ also will apply in the instant proceeding. Though it believes the rate of return will be the same here, if the rate of return in the instant proceeding differs from the rate of return approved in the METC Rate of Return Order for the carrying charge on the deferrals approved in Trans-Elect, METC requests that the Commission clarify that the overall rate of return approved for METC in the METC Rate of Return Order also applies here.²⁶

Commission Determination

45. We will allow Wolverine and MPPA to use the overall rate of return from Attachment O as the carrying charge for their deferrals. Use of the overall rate of return as a carrying charge applied to amounts in the deferral accounts is consistent with our approval in the METC Rate of Return Order. We also clarify that METC's previously approved rate of return will apply to its deferral accounts resulting from the Proposed Settlement Agreement and remains unchanged as a result of this proceeding.

Seven Factor Test

46. In Midwest ISO-Wolverine, the Commission made the following determination related to Wolverine's facilities and the seven factor test:

We agree with the protesters that Wolverine's transmission facilities must meet the requirements of the seven factor test, as interpreted by the Michigan Commission, in order to ensure that Wolverine receives compensation for its transmission facilities on a basis comparable to the compensation received by METC. Application of the seven factor test should form the starting point for these negotiations. (P 21, footnote omitted)

²⁵ For purposes of the deferral account approved in Trans-Elect, the Commission allowed METC to derive its overall rate of return based on the use of: (1) a 13.88 percent ROE; (2) a target capital structure of 50 percent debt and 50 percent equity through December 31, 2004; and (3) METC's actual cost of debt. See, Michigan Electric Transmission Company, LLC, 105 FERC ¶ 61, 214 (2003) (METC Rate of Return Order).

²⁶ METC Comments at 11-12.

47. The Filing Parties submitted a seven factor test performed by GDS Associates, Inc. (GDS).²⁷ GDS concludes that all of Wolverine's non-radial facilities operated at 44kV, 69kV and 138kV, perform transmission functions and should be included in the Joint Zone.

48. Midwest ISO analyzed GDS' study and concluded that it is reasonable to classify all of Wolverine's non-radial 138kV, 44kV, and 69kV facilities as serving a transmission function according to the Commission's seven factor test.

49. Consumers also submitted a seven factor test on Wolverine's facilities, concluding that:

- (1) The Wolverine Airport 138 kV line does perform a transmission function.
- (2) The looped 138 kV portions of the Blendon, Bradley, Oden, Sternberg and Vestaburg substations also perform a transmission function.
- (3) The Wolverine electric system radial 138 kV facilities, 138-69 kV step down transformers, 69 kV facilities, 69-44 kV step down transformers and 44 kV facilities do not perform a transmission function and should be classified as local distribution facilities.

50. Consumers' seven factor test determined that the MPPA member electric systems do not perform a transmission function and should be classified as local distribution facilities.

²⁷ The Filing Parties explain in their filing that, in response to Midwest ISO-Wolverine, Wolverine initially filed an application before the Michigan Commission for an ex parte (no public notice or hearing) determination of the proper classification of its transmission and distribution facilities, which is the procedure used by the Michigan Commission to rule upon most other Michigan utilities' applications for such determination. They go on to explain subsequent events: the Michigan Commission publicly noticed Wolverine's filing and invited comments on whether to hold a hearing on Wolverine's application; comments were received by the Michigan Commission requesting a hearing; the Michigan Attorney General also filed comments explaining that the Michigan Commission had no jurisdiction over Wolverine and could not consider Wolverine's application, regardless of Wolverine's request; on May 12, 2003, the Michigan Commission issued a notice setting Wolverine's application for hearing; on May 21, 2003, Wolverine filed a "Notice of Withdrawal," which the Michigan Commission denied on June 5, 2003; on August 26, 2003, the Michigan Commission dismissed Wolverine's application.

51. The Michigan Commission explains in its August 26 Order that since the Commission expressed interest in having its interpretation of the seven factor test applied to Wolverine's facilities it reviewed the record and determined the appropriate characterization of Wolverine's facilities, notwithstanding the dismissal of Wolverine's application. The Michigan Commission's conclusions are the same as those submitted by Consumers.

52. Neither the Filing Parties nor the Michigan Commission performed a seven factor test on the MPPA facilities, but the Proposed Settlement Agreement states that the transmission facilities of MPPA and those of its member systems are those facilities which are accepted as transmission facilities by Midwest ISO employing the seven factor test. The Proposed Settlement Agreement also states that the initial allocation of MPPA's facilities to the Joint Zone is on a basis such that MPPA will receive compensation that is comparable to that received by METC and Wolverine.

Commission Determination

53. We believe that it is important that Wolverine and MPPA (participants in the joint pricing zone with METC) be compensated for their transmission facilities on a basis comparable to the compensation received by METC. This comparability requires that all of the facilities included in the Joint Zone be classified as transmission facilities with similar application of the seven factor test. We note that it was the Michigan Commission that performed the seven factor test that was used by the Commission to classify the facilities now owned by METC.²⁸ Therefore, we find it is reasonable, as we did in Midwest ISO-Wolverine, to require that other facilities in the Joint Zone with METC meet the requirements of the seven factor test as applied by the Michigan Commission to classify the facilities now owned by METC. The combined nature of the Joint Zone here justifies our giving considerable weight to the Michigan Commission's application of the seven factor test.

54. We reviewed the Michigan Commission's August 26 Order and we believe the conclusion reached in classifying Wolverine's facilities is comparable to the conclusion reached when the Michigan Commission classified the METC (formerly Consumers) facilities. The seven factor test as interpreted in the GDS study may be appropriate under different circumstances; however we reiterate that comparability of facilities is the key factor here because the relevant facilities are part of a joint pricing zone and not a single pricing zone. We emphasize that we are accepting the conclusions of the seven factor test

²⁸ See, unpublished Commission Letter Order dated July 29, 1998, in Docket No. EL98-21-000.

as interpreted by the Michigan Commission here for pricing purposes in the Joint Zone because of the decisions already made regarding pricing for the METC system. We are making no determination as to how we will perform or interpret the seven factor test for purposes other than those presented to us in the instant case.²⁹

55. We understand that our decision causes certain facilities that will be part of the Joint Zone to be different than those contemplated in the Proposed Settlement Agreement. However, the major aspects of the Proposed Settlement Agreement remain intact, including the mechanism for all members of the Joint Zone to receive equitable compensation for the facilities that are included in the Joint Zone.

56. We also believe that MPPA and other entities not subject to Commission or state regulation should have Midwest ISO perform a seven factor analysis to determine what facilities are eligible for inclusion in the Joint Zone, as contemplated in the Proposed Settlement Agreement. However, we note that any such determination is required to be submitted to the Commission when Midwest ISO files amendments to incorporate the new facilities and at that time, we will determine if all the transmission owners within the Joint Zone are compensated on a comparable and equitable basis.

Request For Rehearing

57. The Explanatory Statement states that Wolverine's pending rehearing request will be deemed withdrawn upon issuance of a final order approving the Proposed Settlement Agreement without modification. As discussed above, we are requiring modifications to the Proposed Settlement Agreement. Therefore, we will defer further action on Wolverine's rehearing request submitted in Docket No. ER02-2458-001 until we receive notification from Wolverine as to the status of such request.

²⁹ We reiterate that it is our policy, absent extraordinary circumstances, to defer to state regulatory authorities concerning certain transmission/local distribution matters that arise when retail wheeling occurs, however, “to the extent that any facilities, regardless of their original nominal classification, in fact, prove to be used by public utilities to provide transmission service in interstate commerce . . . such facilities become subject to this Commission’s jurisdiction and review.” See e.g., *MidAmerican Energy Company, et al.*, 90 FERC ¶ 61,105 at 61,337 (2000).

The Commission orders:

- (A) The Michigan Commission's late motion to intervene is hereby denied.
- (B) The Michigan Commission's motion to lodge its Administrative Decision is hereby granted.
- (C) The contested Offer of Settlement is hereby approved, subject to the discussion herein and the filing ordered below.
- (D) The Filing Parties are hereby ordered to file tariff sheets that are consistent with this order and the Commission's rules and regulations, within thirty days of the date of this order.

By the Commission. Commissioner Brownell concurring with a separate statement attached.

(S E A L)

Magalie R. Salas,
Secretary.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Midwest Independent Transmission
System Operator, Inc.

Docket Nos. ER02-2458-000
ER02-2458-001

(Issued March 4, 2004)

Nora Mead BROWNELL, Commissioner *concurring*:

1. This order accepts an amendment to the Proposed Settlement Agreement offered by Wolverine in response to a comment by Trial Staff. The order notes that Trial Staff expressed concern that holding the Commission to the Mobile-Sierra public interest standard of review for subsequent changes would somehow compromise the Commission's ability to protect the public interest. In reaction to Trial Staff's comment, Wolverine stated that the parties had not intended to so bind the Commission and proposed certain amendatory language to clarify this point. The order accepts the amendment.
2. I wish to make clear that I do not believe that holding the Commission to the Mobile-Sierra standard in any way compromises our ability to protect the public interest. As I have said in prior separate statements, I believe that application of the Mobile-Sierra doctrine provides the contract certainty needed to ensure investment while simultaneously protecting the public from unintended consequences when the circumstances surrounding private contracts have changed. See e.g., Midwest Independent Transmission System Operator, Inc., 105 FERC ¶ 61,073 (2003). Moreover, the Commission has been accepting settlement language holding itself to the public interest standard since July 2003. See, e.g., Duke Energy Corporation, 104 FERC ¶ 61,048 (2003).
3. Further, I am comfortable reserving the Commission's option of making subsequent changes to a settlement under the just and reasonable standard, but only if that is the intent of the parties, articulated in explicit language. Here, Wolverine proposed the new language only after Trial Staff raised its concern. Further, Wolverine's proposed language speaks only of the standard applicable to signatories; it remains silent as to the standard applicable to changes sought by the Commission. Therefore, I would have

preferred that we: 1) reject the language offered by Wolverine; and 2) tell the signatories that they may, if they wish, allow for Commission-sought changes under the just and reasonable standard, but only if they file explicit language addressing such changes.

Nora Mead Brownell