

129 FERC ¶ 61,242  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Sudeen G. Kelly, Marc Spitzer,  
and Philip D. Moeller.

Citizens Energy Corporation

Docket No. EL10-3-000

ORDER ON TRANSMISSION RATE INCENTIVES  
AND CAPITAL COST RECOVERY METHODOLOGY

(Issued December 17, 2009)

1. On October 9, 2009, Citizens Energy Corporation (Citizens) filed a petition for a declaratory order pursuant to section 219 of the Federal Power Act<sup>1</sup> and Order No. 679<sup>2</sup> seeking approval of two rate treatments in connection with the proposed transmission project (Project) to deliver renewable resources from Imperial Valley, California to San Diego County, California.<sup>3</sup> As discussed herein, we grant Citizens' request to recover prudently incurred abandonment costs if the Project is abandoned for reasons beyond Citizens' control. We also find that Citizens' capital cost recovery methodology, which includes a hypothetical capital structure of 50 percent debt and 50 percent equity and a 30-year levelized capital recovery approach, will produce just and reasonable results.

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<sup>1</sup> 16 U.S.C. § 824s (2006).

<sup>2</sup> *Promoting Transmission Investment through Pricing Reform*, Order No. 679, FERC Stats. & Regs. ¶ 31,222 (2006), *order on reh'g*, Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 (2006), *order on reh'g*, 119 FERC ¶ 61,062 (2007).

<sup>3</sup> The Project is part of a much larger transmission infrastructure improvement plan in southern California that is being developed by San Diego Gas & Electric Company (SDG&E), known as the Sunrise Powerlink Project. However, the petition pertains only to the portion of the Sunrise Powerlink Project located in Imperial Valley, California, which has been denominated in the petition as the Border-East Line. Accordingly, this order is limited to the proposed capital cost recovery by Citizens of its participation in the Project.

However, as acknowledged by Citizens, the inputs to or components of its proposed formula rate, are subject to a future filing under section 205 of the Federal Power Act.<sup>4</sup>

## **I. Background**

2. The Project is part of a venture with SDG&E, which will deliver up to 1,000 MW of new transfer capacity into the San Diego area from the Imperial Valley and facilitate the development of and provide market access for 1,900 MW of renewable resources in the Imperial Valley region.<sup>5</sup>

3. Citizens notes that while the Project is physically located in Imperial Valley, it will provide reliability and congestion benefits to San Diego County as part of the larger Sunrise Powerlink Project. San Diego County has been designated as a National Interest Electric Transmission Corridor by the U.S. Department of Energy. Citizens also asserts that the Project will allow California utilities to meet their state's 33 percent Renewable Portfolio Standard goal by 2020 at a lower cost than other alternatives that were evaluated.<sup>6</sup> Citizens estimates the total cost of development and construction of the Project is approximately \$166 million.<sup>7</sup>

4. Citizens and SDG&E have entered into an agreement to coordinate and develop the Project. The agreement provides that while SDG&E is responsible for the development and construction of the Project, Citizens will acquire one half of the transfer capability of the Project for a period of 30 years in exchange for financing one-half of the Project's costs—that is, an estimated \$83 million.<sup>8</sup>

5. According to Citizens, the Project has been approved by the California Independent System Operator, Inc.'s (CAISO) transmission planning process and has received a certificate of public convenience and necessity from the California Public Utility Commission (CPUC) to build the Project.<sup>9</sup> As noted in the petition, the CAISO

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<sup>4</sup> 16 U.S.C. § 824d (2006).

<sup>5</sup> The Sunrise Powerlink Project includes three segments: (1) the Project (i.e., the Imperial County 500 kV Link); (2) the San Diego 500 kV Link; and (3) the San Diego County 230 kV Link. *See* Citizens October 9, 2009 Petition at 24 (Citizens Petition).

<sup>6</sup> Citizens Petition at 24-25.

<sup>7</sup> Citizens Petition, Ex. CEC-2 at ¶ 29.

<sup>8</sup> *Id.*

<sup>9</sup> Citizens Petition at 46.

Board of Governors specifically found the Project “as a necessary and cost effective upgrade to the CAISO Controlled Grid that will also facilitate compliance with California renewable energy requirements . . .”<sup>10</sup> and will provide “significant reliability benefits to San Diego, Imperial Valley and Southern California in general by bolstering a weak link in the transmission network.”<sup>11</sup>

6. The Project is currently in the final stages of environmental compliance and permitting before various governmental agencies, including the United States Bureau of Land Management and the United States Forest Service. Citizens anticipates that construction will begin in the next several months, and the Project is expected to be operational by June 2012.<sup>12</sup>

7. Citizens requests authorization to recover 100 percent of all prudently incurred development and construction costs in the event the Project is abandoned as a result of factors beyond Citizens’ control. It also seeks approval of a capital cost recovery methodology, which includes: (i) a hypothetical capital structure of 50 percent debt and 50 percent equity; (ii) the ability to recover capital cost requirements by using a 30-year levelized rate approach; and (iii) a proxy rate of return on equity based on SDG&E’s current return on equity of 11.35 percent. Citizens states that its requested approach for capital cost recovery will lock-in the fixed return levels for both debt and equity components for the full 30-year term of Citizens’ participation in the Project.

8. Citizens asserts that pre-approval of its proposed capital cost recovery under a formula rate is essential for Citizens’ financing. Citizens also states that it intends to finance its participation in the Project using 100 percent debt. However, Citizens is seeking capital costs recovery based upon a hypothetical capital structure and a proxy

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<sup>10</sup> *Id.* at 53.

<sup>11</sup> Press Release, California ISO, California ISO Board Approves Sunrise/Greenpath Transmission Project (Aug. 3, 2006), *available at* <http://www.caiso.com/1847/1847bb8a57f70.pdf>; *see also* Citizens Petition, Ex. CEC-2, Attachment B at 4 (where the Vice President of Planning and Infrastructure Development of CAISO found the Project would increase reliability of the Southern California transmission network); *In re San Diego Gas & Elec. Co.*, Decision No. 08-12-058, at 5 (CPUC Dec. 18, 2008) (finding that the Sunrise Powerlink Project, which includes the Project, will provide over \$200 million per year of reliability benefits and create a more robust southern California transmission system, and provide insurance against unexpected high load growth).

<sup>12</sup> Citizens Petition at 30; Citizens Petition, Ex. CEC-2 at ¶ 35.

rate of return method similar to that utilized by municipal electric utility participants in the CAISO.

## **II. Notice of the Filing and Responsive Pleadings**

9. Notice of Citizens' petition for a declaratory order was published in the *Federal Register*, 74 Fed. Reg. 54,033 (2009), with interventions and protests due on or before November 9, 2009.

10. The CPUC filed a notice of intervention. Timely motions to intervene were filed by the Cities of Santa Clara and Redding, California, and M-S-R Public Power Agency; the Northern California Power Agency; Transmission Agency of Northern California; Metropolitan Water District of Southern California; Modesto Irrigation District; the Sacramento Municipal Utility District; Imperial Irrigation District; the Cities of Anaheim, Azusa, Banning, Colton, Pasadena, and Riverside, California (Six Cities); Pacific Gas & Electric Company; Southern California Edison Company; and SDG&E. In addition, timely comments and protests were filed by Six Cities and Imperial Irrigation District. California Municipal Utilities Association filed a late motion to intervene. Citizens filed an answer to the comments.

## **III. Discussion**

### **A. Procedural Matters**

11. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,<sup>13</sup> the notices of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. In view of the early stage of this proceeding, the parties' interests and the interests they represent, and the absence of undue prejudice or delay, the Commission grants the late-filed motion to intervene submitted by California Municipal Utilities Association pursuant to Rule 214(d) of the Commission's Rules of Practice and Procedure.<sup>14</sup>

12. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure<sup>15</sup> prohibits an answer to a protest or an answer to an answer, unless otherwise ordered by the decisional authority. We will accept Citizens' answer because it has provided information that assisted us in our decision-making process.

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<sup>13</sup> 18 C.F.R. § 385.214 (2009).

<sup>14</sup> *Id.* § 385.214(d).

<sup>15</sup> *Id.* § 385.213(a)(2).

**B. Recovery of Abandoned Costs**

13. We grant Citizens request to recover prudently incurred development and construction costs if the Project is cancelled or abandoned as a result of factors beyond Citizens' control, subject to a subsequent section 205 filing. We note that no party protested Citizens' request for abandoned plant and, as set forth herein, we find the request to be reasonable.

14. To receive transmission infrastructure incentives under section 219, Order No. 679 requires a petitioner to meet a two-prong test. First, an applicant must demonstrate that the facilities for which it seeks incentives either ensure reliability or reduce the cost of delivered power by reducing transmission congestion.<sup>16</sup> Second, the petitioner must demonstrate that there is a nexus between the incentive sought and the investment being made. As we clarified in Order No. 679-A, the nexus test is met when an applicant demonstrates that the total package of incentives requested is "tailored to address the demonstrable risks or challenges faced by the applicant."<sup>17</sup>

15. With regard to the first prong, Order No. 679 stated that an applicant will be entitled to a rebuttable presumption that the project ensures reliability or reduces congestion if: (1) the transmission project results from a fair and open regional planning process that considers and evaluates projects for reliability and/or congestion and is found to be acceptable to the Commission; or (2) the transmission project has received construction approval from an appropriate state commission or state siting authority.<sup>18</sup> However, as Order No. 679-A made clear, a petitioner is entitled to the rebuttable presumption only if it shows that the relevant regional planning process or state commission specifically considered whether the project ensures reliability or reduces the cost of delivered power by reducing congestion.<sup>19</sup>

16. Here, we find that Citizens is entitled to a rebuttable presumption on eligibility for the requested incentive under Order No. 679. As Citizens describes in its petition, the Project has been approved by the CAISO's transmission planning process and received a certificate of public convenience and necessity from the CPUC.<sup>20</sup> These planning processes specifically considered and found that the Project will provide reliability

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<sup>16</sup> *Id.* § 35.35(i).

<sup>17</sup> Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 40.

<sup>18</sup> Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 58.

<sup>19</sup> Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 49.

<sup>20</sup> Citizens Petition at 46.

benefits to the region.<sup>21</sup> Accordingly, we find that Citizens satisfies the first prong under Order No. 679 and section 219.

17. With regard to the second prong, we find that Citizens has shown a nexus between the requested incentive and the investment being made. As we have stated in other cases, the question of whether a project is “routine” is particularly probative to our nexus analysis.<sup>22</sup> To determine whether a project is routine, we examine such factors as: (1) the scope of the project (e.g., dollar investment, increase in transfer capability, involvement of multiple entities or jurisdictions, size, effect on region); (2) the effect of the project (e.g., improving reliability or reducing congestion costs); and (3) the challenges or risks faced by the project (e.g., siting, internal competition for financing with other projects, long lead times, regulatory and political risks, specific financing challenges, other impediments).<sup>23</sup> The Commission also explained that when an applicant has adequately demonstrated that the project for which it requests an incentive is not routine, the applicant has shown, for purposes of the nexus test, that the project faces risks and challenges that merit an incentive.<sup>24</sup>

18. We find that the Project is not routine for purposes of our nexus analysis. Several considerations lead us to this conclusion. For example, the cost of the Project as compared to Citizens’ size supports a finding that the Project is not routine. Specifically, as Citizens emphasizes in its petition, the projected investment of \$83 million by Citizens will exceed its net asset value of \$50 million and represents a major capital commitment for a company the size of Citizens.<sup>25</sup> In addition, Citizens explains in its petition how the Project will facilitate compliance with California’s renewable energy requirements. The Commission has previously found that construction of transmission facilities designed to provide access to remote renewable energy resources is not routine.<sup>26</sup>

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<sup>21</sup> See *supra* note 11.

<sup>22</sup> *Baltimore Gas and Elec. Co.*, 120 FERC ¶ 61,084, at P 48 (2007), 121 FERC ¶ 61,167, *reh’g denied*, 122 FERC ¶ 61,034 (2007), *reh’g denied*, 123 FERC ¶ 61,262 (2008).

<sup>23</sup> *Id.* P 52-55.

<sup>24</sup> *Id.* P 54.

<sup>25</sup> We have previously found that the cost ratio is a significant factor in determining whether a project is routine. See, e.g., *Tallgrass Transmission, LLC*, 125 FERC ¶ 61,248, at P 56 (2008); *PacifiCorp*, 125 FERC ¶ 61,076, at P 44 (2008).

<sup>26</sup> See, e.g., *PacifiCorp*, 125 FERC ¶ 61,076 at P 45 (2008); *Green Energy Express LLC*, 129 FERC ¶ 61,165 at P 33 (2009).

19. Accordingly, we believe Citizens has satisfied the requirements of section 219 and Order No. 679. As such, we will grant Citizens' request for recovery of 100 percent of prudently incurred costs if the Project is abandoned for reasons beyond Citizens' control. Consistent with Commission policy, however, Citizens' recovery of any future abandonment costs is subject to a future section 205 filing where Citizens must demonstrate that the costs are just and reasonable.

### **C. Capital Cost Recovery Methodology**

#### **1. Comments and Protests**

20. Six Cities and Imperial Irrigation District request clarification that any approval of Citizens' requested rate methodology does not constitute pre-approval of any component of or input to any formula rate to be filed by Citizens in the future or of the capital lease to be developed by Citizens and SDG&E or of any other possible projects in which Citizens may become involved. In addition, Six Cities requests a detailed explanation and justification by Citizens for its proposed 30-year capital recovery period.<sup>27</sup> Six Cities notes that Citizens' application acknowledges that the expected useful life of the Project facilities is 58 years and Citizens has provided no explanation as to why transmission customers should be required to provide full recovery of the capital investment over a period shorter than the expected life.

#### **2. Citizens' Answer**

21. Citizens emphasizes that it does not seek pre-approval for any component or input to a formula rate, but rather seeks pre-approval of its proposed capital cost recovery methodology.<sup>28</sup> Citizens also emphasizes the importance of the proposed 30-year period of recovery of its capital costs. Citizens asserts that its 30-year fixed cost debt financing arrangement "was determined to be optimal as it would enable low cost borrowing on a levelized repayment basis over a conventional long term maturity period acceptable to utility debt investors."<sup>29</sup> Citizens states that a longer repayment period may not be feasible under prevailing financial circumstances and would be more costly. Citizens also notes that the 30-year fixed long-term debt financing would allow it to lock-in this major cost component on a fixed, levelized basis, which in turn would protect consumers against inflationary and monetary cost risks over time. Finally, Citizens asserts consumers are protected against any higher cost burden that would occur over a 58-year recovery because Citizens has committed in its agreement with SDG&E that its fixed rate

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<sup>27</sup> See Six Cities November 9, 2009 Comments at 3.

<sup>28</sup> Citizens November 11, 2009 Answer at 1 n.1 (Citizens Answer).

<sup>29</sup> *Id.* at 3.

for capital requirements cost will be no greater than the rate that SDG&E would charge for Citizens' interest in the Project.<sup>30</sup>

### 3. Commission Determination

22. The Commission finds that Citizens' capital cost recovery methodology, including its request to use a hypothetical capital structure of 50 percent debt and 50 percent equity and a 30-year levelized fixed rate of recovery of capital requirements, is reasonable in this context. The Commission has previously approved a hypothetical capital structure of 50 percent debt and 50 percent equity in relation to other transmission construction projects.<sup>31</sup> We also have permitted other entities, such as municipals, to use a hypothetical capital structure for ratemaking purposes when they have relied upon non-equity financing to finance a project, as Citizens proposes to do here.<sup>32</sup> In addition, as Citizens notes, the hypothetical capital structure of 50 percent debt and 50 percent equity is less than SDG&E's current equity rate of 55 percent.

23. We also find that the 30-year levelized fixed rate of recovery of capital requirements requested by Citizens is reasonable.<sup>33</sup> In support of its use of a levelized approach, Citizens states that because the transmission benefits of the Project will be constant over time, the "front-end loading" of cost recovery under traditional cost of service ratemaking would mismatch Project benefits with costs. We find that Citizens proposed levelized approach is reasonable in the context of rate recovery for a single asset and will ensure a constant revenue stream.

24. Contrary to Six Cities' request, we find it unnecessary to require Citizens to provide additional explanation or justification for the 30-year period. Citizens provided

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<sup>30</sup> *Id.* at 4.

<sup>31</sup> See, e.g., *Trans-Elect NTD Path 15*, 109 FERC ¶ 61,249, at P 26-29 (2004); *Potomac-Appalachian Transmission Highline, LLC*, 122 FERC ¶ 61,188, at P 55 (2008); *Tallgrass Transmission*, 125 FERC ¶ 61,248 at P 68; *Pioneer Transmission, LLC*, 126 FERC ¶ 61,281, at P 119 (2009).

<sup>32</sup> See *City of Vernon, California*, 109 FERC ¶ 63,057, at P 110-119 (2004), *aff'd*, 111 FERC ¶ 61,092 (2005).

<sup>33</sup> The Commission has approved capital cost recovery periods that were less than the physical life of the facilities. See, e.g., *Westar Energy, Inc.*, 122 FERC ¶ 61,268 (2008) (finding a 15-year accelerated-depreciation schedule to be appropriate).

significant explanation and justification for its request in its petition and its answer.<sup>34</sup> It has supported the use of a 30-year depreciable life by stating that in the current market, the financing of the Project over 30 years is the least cost alternative because it will protect consumers against future inflationary and monetary cost risks. In particular, Citizens notes that an interest rate for a 30-year loan will likely be 6.5 percent, whereas a 58-year loan will likely be 8.5 percent. This difference alone will result in significant savings for consumers. A longer depreciable life, as Citizens argues, will increase the financing costs of the Project and, thus, erode the benefits that will inure to it from the Project. We also note that Citizens and SDG&E have entered into a lease agreement with a 30-year term. Based on these facts, we find that Citizens' request to use a 30-year depreciable life for its capital cost recovery is reasonable in the context of this case.

25. Based on Citizens' answer, we understand that Citizens is not requesting approval of its specific return on equity or the proposed terms of its lease agreement at this time. Therefore, we find that Citizens' return on equity, based on SDG&E's current authorized return on equity of 11.35 percent, is subject to a future section 205 filing. We will not prejudge that return on equity by approving Citizens' proxy rate of 11.35 percent at this time, but instead will review Citizens' requested return when it makes the necessary filing to show that the rate is just and reasonable. We note that this finding is consistent with Citizens' answer in which it stated that it was not seeking pre-approval for any component or input to its formula rate.<sup>35</sup>

26. Finally, Citizens states in its petition that its share of capital contributed to the Project is estimated to be \$83 million and proposes to account for its capital contribution as prepaid leasehold rent.<sup>36</sup> According to Citizens, the rent will be paid in a lump sum and shall be allocated over the lease term. Citizens' future section 205 filing must provide the full particulars of its proposed accounting on all aspects of the capital contribution to the Project and entitlement to a portion of the Project's transfer capabilities, together with narrative explanations describing the basis for the lease accounting for book purposes.

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<sup>34</sup> Citizens Petition at 38-43; Citizens Petition, Ex. CEC-3 at ¶ 27; Citizens Answer at 2-5.

<sup>35</sup> Citizens Answer at 1 n.1.

<sup>36</sup> Citizens Petition at 27-28; Citizens Petition, Ex. No. CEC-3 at ¶ 24.

The Commission orders:

Citizens' petition for declaratory order is hereby granted, as discussed in the body of this order.

By the Commission.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.