

125 FERC ¶ 61,341
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeem G. Kelly, Marc Spitzer,
and Jon Wellinghoff.

American Electric Power Service Corporation v. Docket No. EL07-101-001
Midwest Independent Transmission System Operator,
Inc. and PJM Interconnection, L.L.C.

Midwest Independent Transmission System Operator, Docket No. ER05-6-103
Inc.

Midwest Independent Transmission System Operator, Docket No. EL04-135-106
Inc., PJM Interconnection, L.L.C.

Midwest Independent Transmission System Operator, Docket No. EL02-111-123
Inc., PJM Interconnection, L.L.C.

Ameren Services Company Docket No. EL03-212-119

ORDER ON REHEARING

(Issued December 19, 2008)

1. In an order issued January 31, 2008, the Commission denied American Electric Power Service Corporation's (AEP) complaint,¹ filed pursuant to sections 206 and 306 of the Federal Power Act (FPA)² and Rule 206 of the Commission's Rules of Practice and

¹ AEP filed its complaint on behalf of certain operating companies of the American Electric Power System (Appalachian Power Company, Columbus Southern Power Company, Indiana Michigan Power Company, Kentucky Power Company, Kingsport Power Company, Ohio Power Company and Wheeling Power Company).

² 16 U.S.C. §§ 824e, 825e (2006).

Procedure,³ against Midwest Independent Transmission System Operator, Inc. (Midwest ISO) and PJM Interconnection, L.L.C. (PJM) challenging the justness and reasonableness of the rate designs underlying the Midwest ISO and PJM open access transmission tariffs (tariffs).⁴ For the reasons discussed below, we deny the request for rehearing of the January 31 Order.

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³ 18 C.F.R. § 385.206 (2008).

⁴ *American Electric Power Service Corporation*, 122 FERC ¶ 61,083 (2008) (January 31 Order).

I. Background**A. Existing PJM and Midwest ISO Rate Design⁵****1. Intra-RTO Rates****a. Intra-PJM Rate Design**

2. The Commission allowed PJM to charge license-plate rates to recover the cost of all transmission facilities for service within PJM for an initial fixed period that expired on June 1, 2005, pursuant to the terms of a settlement agreement.⁶ The Commission also allowed PJM to use a “beneficiary pays” approach to recover the cost of new facilities. Under this approach, PJM allocated the cost of new facilities based on its independent determination of which loads created the need for or benefited from the new facilities. The Commission required PJM and the PJM transmission owners to file, on or before January 31, 2005, a reevaluation of their intra-Regional Transmission Operator (intra-RTO) rate design, for both new and existing facilities, and propose a rate design to take effect on June 1, 2005. PJM and the PJM transmission owners submitted the required reevaluation and rate design on January 31, 2005, and the Commission set the proposal for hearing.⁷ The Commission ultimately addressed PJM’s rate design in Opinion No. 494.⁸

i. Pricing for Existing Facilities

3. Pursuant to the Commission’s findings in Opinion No. 494, PJM will continue to use license-plate rates to recover the cost of existing transmission facilities.⁹ Under its license-plate rate design, PJM’s footprint is segregated into transmission pricing zones,

⁵ The January 31 Order contained a detailed discussion of the inter- and intra-RTO rate designs and the regulatory history that lead to the existing rate design. *Id.* P 4-29.

⁶ *Allegheny Power Sys. Operating Cos.*, 108 FERC ¶ 61,167 (2004).

⁷ *Allegheny Power Sys. Operating Cos.*, 111 FERC ¶ 61,308 (2005), *order on reh’g*, 115 FERC ¶ 61,156 (2006).

⁸ *PJM Interconnection, L.L.C.*, Opinion No. 494, 119 FERC ¶ 61,063 (2007), *order on reh’g*, Opinion No. 494-A, 122 FERC ¶ 61,082 (2008), *appeal docketed*, *Ill. Commerce Comm. v. FERC*, No. 08-1306 (7th Cir. Feb. 8, 2008).

⁹ There is an exception for 500 kV facilities in the “classic” PJM area where transmission owners have historically shared costs of certain facilities under existing extra-high voltage agreements.

typically based on the boundaries of individual transmission owners or groups of transmission owners. A customer pays a rate that reflects the cost of existing facilities in the pricing zone where its transaction sinks.

ii. Pricing for New Facilities

4. With respect to new facilities, the Commission, in Opinion No. 494, established two approaches based on a voltage threshold. For new reliability facilities built pursuant to PJM's Regional Transmission Expansion Plan (RTEP) and operated below 500 kV, the Commission retained a beneficiary pays approach and directed the parties to develop a specific methodology to include in the PJM tariff as part of the already-established proceeding on the proposed allocation of individual reliability facilities that PJM had filed in Docket No. ER06-456, *et al.* The Commission also initiated, in Docket No. EL07-57, a section 206 investigation of PJM's cost allocation methodology for economic projects below 500 kV for the purpose of developing a specific tariff methodology for determining who benefits from, and thus should pay for, such upgrades.

5. For new facilities operated at or above 500 kV, the Commission in Opinion No. 494 established a regional rate design based on a postage-stamp allocation methodology.¹⁰ The Commission reasoned that a postage-stamp allocation methodology best supports new investment that will strengthen the electric system, improve reliability and support regional markets.

b. Intra-Midwest ISO Rate Design

6. The Commission allowed Midwest ISO to use license-plate rates for the initial six-year transition period ending January 31, 2008. The Commission also allowed Midwest ISO to spread some of the cost of certain new facilities to customers outside a particular zone, as outlined in the Commission orders in the Regional Expansion Criteria and Benefits (RECB) I¹¹ and RECB II¹² proceedings. The Commission required Midwest

¹⁰ Under a postage-stamp rate design, all transmission service customers in a region pay a uniform rate per unit-of-service, based on the aggregate cost of all transmission facilities in the region.

¹¹ *Midwest Indep. Transmission Sys. Operator, Inc.*, 114 FERC ¶ 61,106, *order on reh'g, technical conference and compliance*, 117 FERC ¶ 61,241 (2006), *order on reh'g*, 118 FERC ¶ 61,208 (2007), *aff'd sub nom. Pub. Serv. Comm'n of Wisc. v. FERC*, No. 06-1408 (D.C. Cir. Oct. 31, 2008) (*Pub. Serv. Comm'n of Wisc.*) (collectively, RECB I).

¹² *Midwest Indep. Transmission Sys. Operator, Inc.*, 118 FERC ¶ 61,209, *order on reh'g*, 120 FERC ¶ 61,080 (2007) (collectively, RECB II).

ISO and the Midwest ISO TOs to file, on or before August 1, 2007, a reevaluation of their intra-RTO rate design and to propose a rate design to take effect on February 1, 2008. In response to the required reevaluation of Midwest ISO's intra-RTO rate design, the Commission accepted, in an order issued concurrently with the January 31 Order, a proposal for Midwest ISO to continue using its current intra-RTO rate design after January 31, 2008.¹³

i. Pricing for Existing Facilities

7. Currently, Midwest ISO recovers the cost of existing facilities through zonal license-plate rates. Like PJM, Midwest ISO's footprint is segregated into transmission pricing zones, typically based on the boundaries of individual transmission owners or groups of transmission owners. A customer pays the rate in the pricing zone where its transaction sinks, and that zonal rate recovers the embedded costs of only the existing transmission facilities that are located in that zone.

ii. Pricing for New Facilities

8. Currently, the cost of new reliability facilities planned under the Midwest ISO Regional Transmission Expansion Planning protocols are allocated as outlined in the RECB I proceeding. Under the RECB I process, 20 percent of the cost of qualifying Midwest ISO Regional Transmission Expansion Planning reliability projects rated at or above 345 kV is allocated across the Midwest ISO footprint on a load ratio share basis (i.e., a postage-stamp rate), and the remaining 80 percent of the cost is allocated sub-regionally to one or more zones based on a Line Outage Distribution Factor analysis.¹⁴ For new facilities between 100 kV and 344 kV, 100 percent of cost is allocated sub-regionally, to one or more zones, based on a Line Outage Distribution Factor analysis.

9. The cost of new facilities built for economic (rather than reliability) reasons is allocated as outlined in the RECB II proceeding. Under the RECB II process, 20 percent of the cost of qualifying economic projects¹⁵ is allocated across the Midwest ISO

¹³ *Midwest Indep. Transmission Sys. Operator, Inc.*, 122 FERC ¶ 61,081 (2008).

¹⁴ Qualifying Midwest ISO Regional Transmission Expansion Planning reliability projects must: (1) cost \$5 million or more; or (2) constitute five percent or more of the TO's net plant.

¹⁵ Qualifying economic projects must satisfy two benefits tests. First, the weighted present value sum of a production cost benefit measure (weighted 70 percent) and a Locational Marginal Pricing (LMP)-based energy cost benefit measure (weighted 30 percent), determined in aggregate for all generation and load nodes under the tariff, must be greater than zero. Second, a proposed project must satisfy a variable cost/benefit
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footprint on a load ratio share basis, and the remaining 80 percent is allocated among three geographic subregions based on a beneficiary analysis.¹⁶

10. In accepting Midwest ISO's internal cost allocation proposals for new facilities, the Commission recognized that it had approved different regional postage-stamp cost allocations for new facilities for different regions of the country,¹⁷ but it explained that regional differences may warrant differing levels of regional transmission cost allocation.¹⁸ Additionally, the Commission stated that it viewed the 20 percent postage-

ratio (the weighted sum of the production cost and LMP-based energy cost benefits divided by the project cost) threshold. If the project meets three additional criteria (the project costs more than \$5 million, involves facilities with voltages of 345 kV or higher, and is neither a qualifying reliability project nor a "New Transmission Access" project), then it is eligible for regional cost allocation.

¹⁶ Subregions are assigned costs of eligible economic projects based on the weighted sum of 70 percent of the production cost benefit measure and 30 percent of the LMP-based energy cost benefit measure for each subregion. Once each subregion is assigned its portion of the project cost, the cost allocation to each individual entity within each geographic subregion will be on a load ratio share basis. The methodology provides for a deviation from the above cost allocation when the weighted sum of the production cost benefit and the LMP-based energy cost benefit to any one of the three subregions is negative. That is, a subregion for which the weighted sum of the production cost benefit and LMP-based energy cost benefit is less than zero is not allocated a share of the 80 percent subregional component.

¹⁷ *See, e.g., Sw. Power Pool, Inc.*, 111 FERC ¶ 61,118, at P 25, 31, *order on reh'g*, 112 FERC ¶ 61,319 (2005) (permitting 33 percent of new "Base Plan" upgrades to be allocated on a regional basis); *New England Power Pool and ISO New England, Inc.*, 105 FERC ¶ 61,300, at P 3, 21-23 (2003), *order on reh'g*, 109 FERC ¶ 61,252 (2004) (allowing 100 percent of costs of upgrades rated at 115 kV and above that meet certain non-voltage criteria to be allocated on a regional basis).

¹⁸ For example, in the RECB II proceeding, the Commission stated:

The Commission accepts regional differences in cost allocation and does not mandate a one-size-fits-all approach. . . . [T]here are important differences between the regions. For example, . . . Midwest ISO serves an extremely large footprint that has not, to date, had a history of regional transmission planning or cost allocation. It is therefore neither surprising nor necessarily inappropriate that . . . Midwest ISO's proposal for regional cost allocation would

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stamp rate in Midwest ISO as a first step. The Commission directed Midwest ISO and the Midwest ISO TOs to revisit the 20 percent postage-stamp cost allocation for new facilities when they filed the required August 1, 2007 post-transition rate design for existing transmission facilities.

2. Inter-RTO Rates

11. For inter-RTO service, Midwest ISO and PJM treat transactions that source in one RTO and sink in the other RTO the same as transactions that source and sink entirely in one RTO. These inter-RTO transactions are assessed only the applicable zonal charge of the sink zone; the RTO where these transactions originate does not assess a charge. The Commission required the RTOs and their transmission owners to make a filing to reevaluate the license-plate rate design for inter-RTO service and proposing a rate design to take effect on February 1, 2008. The Commission stated that the required reevaluation “is not a mandate that license plate rates for service between the RTOs must be eliminated at the end of the term.”¹⁹ The Commission also required the RTOs and their transmission owners to address how they would recover the cost of new transmission facilities during the initial fixed period and directed them to develop a joint proposal for allocating to customers in each RTO the cost of new transmission facilities that are built in one RTO but benefit customers in the other (cross-border facilities).²⁰

12. In the January 31 Order, the Commission accepted the Independent RTO Pricing Design, which is the methodology for pricing transmission service between the RTOs that Midwest ISO, PJM and a majority of their member transmission owners proposed in response to the requirement to reevaluate the inter-RTO rate design prior to February 1, 2008.²¹ Under the Independent RTO Pricing Design, the RTOs will maintain the existing

fail to allocate costs as broadly as regions with a smaller footprint and, in the case of New England, a long history of integrated and coordinated operations.

Midwest Indep. Transmission Sys. Operator, Inc., 118 FERC ¶ 61,209 at P 69; *see also* Opinion No. 494, 119 FERC ¶ 61,063 at P 39 (“[T]he Commission has permitted different just and reasonable rate designs reflective of particular system characteristics and stakeholder input. In this regard, we have stated our deference to regional preferences a number of times . . .”).

¹⁹*Midwest Indep. Transmission Sys. Operator, Inc.*, 109 FERC ¶ 61,168, at P 62 (2004).

²⁰*Id.* P 60.

²¹ January 31 Order, 122 FERC ¶ 61,083 at P 163-64.

inter-RTO rate design with no changes. The inter-RTO zonal rates charged under the Independent RTO Pricing Design are the same as the intra-RTO zonal rates in each RTO's tariff and are based on the same cost allocation methodologies established in each RTO for intra-RTO service.

B. Summary of the AEP Complaint

13. On September 17, 2007, AEP filed a complaint alleging that the rate design and cost allocation methodology under the Midwest ISO and PJM tariffs is unjust, unreasonable, unduly discriminatory, and unduly preferential and, therefore, must be revised. In its place, AEP sought a postage-stamp rate design for all new and existing high-voltage facilities across the combined Midwest ISO/PJM region.

14. In its complaint, AEP argued that it has built the most extensive transmission network in the Eastern Interconnection and emphasized the value of the AEP high-voltage system to the combined Midwest ISO/PJM region. AEP argued that: (1) it has the most highly interconnected system in the Eastern Interconnection and has 27 interconnections with Midwest ISO and 12 with PJM, with a combined capability of over 46,200 MW; (2) its high-voltage transmission system enhances regional reliability and protected most of Midwest ISO and the western portion of PJM from the 2003 blackout; and (3) its transmission system provides more benefits to others in the combined Midwest ISO/PJM region than customers in the AEP zone receive from the transmission systems of the Midwest ISO transmission owners and the other PJM transmission owners. AEP asserted that, despite the value of its high-voltage transmission system to the combined Midwest ISO/PJM region and Commission precedent regarding cost allocation in accordance with cost causation, customers outside of the AEP zone do not pay to use the AEP high-voltage system under the existing rate design. AEP further argued that the existing rate design has cost AEP's zonal customers "upwards of \$175 million for existing facilities and tens of millions more in new facilities, resulting in rate increases of some fifty percent."

15. AEP asserted that the Commission and courts recognize generalized benefits as the rationale for socializing costs among various classes of beneficiaries.²² AEP also argued that Commission precedent requires that customers who benefit pay a fair share of costs.²³ Accordingly, AEP asserted that the existing rate design unfairly allocates the

²² *Midwest Indep. Transmission Sys. Operator, Inc.*, 118 FERC ¶ 61,209 at 34-35 (citing, *inter alia*, *Entergy Servs., Inc. v. FERC*, 319 F.3d 536, 543 (D.C. Cir. 2003); *Transmission Owners of the Midwest Indep. Sys. Operator, Inc.*, 110 FERC ¶ 61,339, at P 33-34 (2005)).

²³ *Id.* at 32-33 (citing, *inter alia*, *Midwest ISO Transmission Owners v. FERC*, 373 F.3d 1361, 1368 (D.C. Cir. 2004); *PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,112, (continued)

cost of its high-voltage transmission system exclusively to transmission customers within the AEP footprint while allowing other customers located within Midwest ISO and PJM to avoid paying any of the costs, even though those customers are also beneficiaries of AEP's high-voltage system. AEP argued that whether or not its high-voltage facilities were planned and designed through the RTO planning model "has never been a factor in designing rates for coordination power sales or third-party transmission, as the Commission consistently has recognized that those services are provided over facilities that primarily were planned and designed to serve native load customers."²⁴

16. AEP stated in its complaint that it believes that a common regional rate design is needed for the combined Midwest ISO/PJM region. AEP noted that for allocation purposes, PJM and Midwest ISO slice and dice the costs of transmission facilities in a variety of ways: by region (PJM or Midwest ISO), geographic areas (zones), vintage of facilities (existing or new), size (345 kV and above or lower; 500 kV and above or lower), cost (\$5 million plus or lower), and purpose (reliability or economic).

17. AEP proposed a replacement "highway/byway" rate design that would allocate the costs of both existing and new high-voltage (or "highway") transmission facilities (those facilities operated at 345 kV and above, or alternatively at 765 kV and above) to customers across the entire combined Midwest ISO/PJM region on a postage-stamp basis. AEP argued that under its proposal, all customers that benefit from the use of Midwest ISO and PJM combined backbone transmission facilities will share the burden of the costs. For existing and new lower voltage (or "byway") transmission facilities within the combined Midwest ISO/PJM region, AEP proposed to maintain the current allocation methodology. AEP asked the Commission to initiate hearing procedures to consider its proposed rate design for transmission service in the combined Midwest ISO/PJM region.

18. In anticipation of claims that the Commission already rejected AEP's arguments in Opinion No. 494, AEP stated that Opinion No. 494 does not preclude an inquiry into the lawfulness of the rate design for the combined Midwest ISO/PJM region because that proceeding focused on PJM alone, while the AEP Complaint concerns the combined Midwest ISO/PJM region. AEP also noted that the Commission previously declined to terminate or expand the scope of the PJM-only proceeding and stated that the PJM-only proceeding should remain separate and apart from an analysis of how costs are allocated among the Midwest ISO transmission owners and the PJM transmission owners.

at P 22 (2004); *Cal. Indep. Sys. Operator Corp.*, 106 FERC ¶ 61,032, at P 10 (2004), *order on reh'g*, 113 FERC ¶ 61,135 (2005)).

²⁴ *Id.* at 23.

C. January 31 Order

19. In the January 31 Order, the Commission denied AEP's complaint, finding that AEP had raised many of the same arguments it had raised, and the Commission had rejected, in the Opinion No. 494 proceeding.²⁵ The Commission found that AEP had failed to meet its burden to show that the existing rate design in Midwest ISO and PJM is unjust and unreasonable.²⁶

II. Rehearing Request and Responsive Pleadings

20. On March 3, 2008, AEP filed its request for rehearing. On March 18, 2008, Responding Transmission Owners²⁷ filed an answer. On April 2, 2008 AEP filed an answer to Responding Transmission Owners' answer.

III. Procedural Matters

21. Rule 713(d)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d)(1) (2008), prohibits answers to requests for rehearing. Accordingly, we will

²⁵ January 31 Order, 122 FERC ¶ 61,083 at P 72.

²⁶ *Id.* P 88.

²⁷ Responding Transmission Owners include: Pepco Holdings, Inc. transmission-owning affiliates Potomac Electric Power Company, Delmarva Power & Light Company, and Atlantic City Electric Company; PPL Electric Utilities Corporation; Public Service Electric and Gas Company; Virginia Electric and Power Company, doing business as Dominion Virginia Power; Jersey Central Power & Light Company, Metropolitan Edison Company, and Pennsylvania Electric Company, all subsidiaries of FirstEnergy Corp; and the following Midwest ISO Transmission Owners: City of Columbia Water and Light Department (Columbia, MO); City Water, Light & Power (Springfield, IL); Duke Energy Shared Services for Duke Energy Ohio, Inc., Duke Energy Indiana, Inc., and Duke Energy Kentucky, Inc.; Great River Energy; Indianapolis Power & Light Company; Michigan Public Power Agency; Minnesota Power (and its subsidiary Superior Water, L&P); Montana-Dakota Utilities Co.; Northern Indiana Public Service Company; Northern States Power Company, a Minnesota corporation, and Northern States Power Company, a Wisconsin corporation, subsidiaries of Xcel Energy Inc.; Northwestern Wisconsin Electric Company; Otter Tail Power Company; Southern Illinois Power Cooperative; Southern Indiana Gas & Electric Company; Southern Minnesota Municipal Power Agency; Wabash Valley Power Association, Inc.; and American Transmission Systems, Incorporated, a subsidiary of FirstEnergy Corp.

reject Responding Transmission Owners' answer to the request for rehearing of AEP and AEP's answer to Responding Transmission Owners.

IV. Discussion

A. Burden to Establish a *Prima Facie* Case

1. January 31 Order

22. In the January 31 Order, the Commission found that AEP had failed to meet its burden to establish a *prima facie* case that the current rate designs in Midwest ISO and PJM (and therefore, the inter-RTO rate design) are unjust and unreasonable.²⁸

2. Request for Rehearing

23. On rehearing, AEP argues that the Commission erred by focusing on the alleged impacts of AEP's proposal as a basis for affirming the current rate structure, thereby conflating the two separate and distinct responsibilities under FPA section 206. AEP argues that the courts have emphasized that under the two-step process required by the statutory language, the Commission's analysis necessarily must focus initially on whether the existing rates fairly and appropriately allocate the costs of the regional grid among the users of the grid. AEP asserts that only after completing that analysis should the Commission turn to the appropriate replacement rate.

24. AEP also disagrees with the January 31 Order's conclusion that its evidence fails to present a *prima facie* case. AEP argues that it has presented sufficient evidence to support its claim that existing rates are unjust and unreasonable, but that the Commission has erred in analyzing this evidence and erroneously concluding that AEP failed to meet its burden.

3. Commission Determination

25. We deny AEP's request for rehearing. AEP asserts that we relied on the impacts of its alternative proposal as a basis for affirming the existing rate design in the January 31 Order. However, we stated in the January 31 Order that under FPA section 206, AEP, as the proponent of the rate design change, bears the burden of showing that the existing rate design is unjust and unreasonable.²⁹ We did not substantively assess AEP's

²⁸ January 31 Order, 122 FERC ¶ 61,083 at P 88.

²⁹ *Id.* (citing "*Complex*" *Consol. Edison Co. of N.Y., Inc. v. FERC*, 165 F.3d 992, 1000-02 (D.C. Cir. 1999) (citing *Tenn. Gas Pipeline Co.*, 80 FERC ¶ 61,070 (1997)) (analyzing the comparable provisions sections 4 and 5 of the Natural Gas Act (NGA))).

alternative proposal in the January 31 Order, finding instead that AEP had failed to show that the existing rate design in the combined Midwest ISO/PJM area is unjust and unreasonable.³⁰

26. As the courts have found, on the same set of facts there can be “multiple just and reasonable rates” and the resolution may depend on whether the proceeding is initiated under section 206.³¹ There is no identifiable threshold at which a particular rate design becomes unjust and unreasonable.³²

27. While there is no bright-line test for determining whether AEP has met its burden, we find that AEP’s conclusory assertion that it has presented sufficient evidence to support its claim that existing rates are unjust and unreasonable is insufficient. As discussed below, we reject AEP’s arguments that the existing inter-RTO rate design is unjust and unreasonable. Because we find AEP’s arguments to be without merit, we find that AEP has not met its burden to establish a *prima facie* case.

B. Existing vs. New Facilities

1. January 31 Order

28. In the January 31 Order, the Commission rejected AEP’s complaint, in which AEP asserted that the existing inter-RTO rate design is unduly discriminatory and preferential because the costs of all existing transmission facilities are allocated to the customers within the zone where the facilities are located, while the costs of new high-voltage facilities are allocated on a regional basis (through various methods) and proportionally added to each zone’s rate. AEP claimed that the Commission should require that the cost of its existing high-voltage facilities be spread across the entire combined Midwest ISO/PJM region because of the role that AEP’s existing high-voltage facilities play in integrating the two RTOs, in permitting customers to reap the benefits of that integration, and in facilitating the major new high-voltage projects that are planned for the combined region.

³⁰ *See infra* P 81-82.

³¹ January 31 Order, 122 FERC ¶ 61,083 at P 88.

³² *Id.* (citing *Tenn. Gas Pipeline Co.*, 80 FERC at 61,224 (finding “there is not a single magic point on the continuum between incremental and rolled-in rates such that at that single point an incremental rate becomes unjust and unreasonable while a rolled-in rate simultaneously becomes just and reasonable”)).

29. The Commission found that, in the context of the rate design for service between Midwest ISO and PJM, license-plate rates continue to be a just and reasonable method to recover the cost of existing facilities.³³ The Commission also found it reasonable for the RTOs to maintain differing treatment of new and existing facilities because there are fundamental differences between these facilities. The Commission noted that Midwest ISO and PJM plan the construction of new facilities based on each RTO's independent planning process, whereas decisions to build existing facilities were not made as part of any regional planning process. The Commission also stated that unlike existing facilities, the rate design for new facilities has efficiency implications.

30. The Commission stated in the January 31 Order that, unlike existing facilities, the rate design for new facilities has efficiency implications. The Commission found that reallocating the cost of existing facilities would neither provide economic efficiencies nor promote the goal of increasing necessary transmission investment.³⁴

2. Rehearing Request

31. AEP argues that the Commission's reliance on policy arguments in the January 31 Order was not the product of reasoned decision-making and that the order is not supported by substantial evidence. In particular, AEP asserts that the distinction between new and old facilities is not relevant to cost allocation issues. That certain facilities were not constructed under a regional planning process says nothing about the benefits that they currently bring to the region, according to AEP. AEP argues that the real-world benefits provided by its existing transmission facilities and currently enjoyed by users across the region cannot be dismissed out of hand because the facilities that provide the current benefits were built before PJM and Midwest ISO undertook responsibility for regional planning.

32. AEP argues that although the January 31 Order emphasizes that an RTO is a "network of interrelated transmission" systems, suggesting that the members receive reciprocal benefits from using each others' systems, the record contains no evidence demonstrating that the region's transmission systems are of comparable size and provide fairly comparable levels of third-party service. AEP asserts that the record shows just the opposite. According to AEP, its existing facilities provide real-world benefits because they annually carry upwards of 80 million MWhs to loads throughout PJM and Midwest ISO; they provide the essential backbone of the region's transmission grid; they serve as the primary tie between disparate Midwest ISO regions and between Midwest ISO and PJM; there would be virtually no transfer capability across the region without these

³³ January 31 Order, 122 FERC ¶ 61,083 at P 95.

³⁴ *Id.* P 97.

facilities; and at least six of the major new extra high voltage projects planned for the region will interconnect with and directly depend upon AEP's existing extra high voltage network. In addition, AEP states that the PJM-Midwest ISO Joint Operating Agreement (JOA) confirms that the PJM and Midwest ISO markets depend heavily on AEP's existing transmission system since a substantial portion of AEP flowgate capacity is allocated to Midwest ISO.

33. AEP also argues that the January 31 Order conflicts with Order No. 2000 because the Commission disregarded consideration of region specific factors, such as the geographic makeup of the RTO. AEP asserts that in Order No. 2000, the Commission made clear that a decision as to whether to allow the continuation of license plate rates would be based on consideration of region-specific factors, such as the geographic makeup of the RTO. AEP states that it submitted evidence to show that its system is unique in the region, in that it serves as the primary gateway enabling lower-cost energy in western PJM and Midwest ISO to displace higher-cost energy in eastern and northern parts of the region.

34. AEP also asserts that the Commission in the January 31 Order disregards the Commission's prior findings that AEP's facilities are integrated with and integral to the regional markets. AEP further argues that the Commission has consistently required third-party users to contribute to the fixed costs of facilities built to serve native load. AEP states that the Commission has always required that customers taking through-and-out service bear an appropriate share of transmission system costs to compensate for the use made and benefits enjoyed by their use of the system. AEP also argues that these principles have been applied in the context of pricing power sales from generation assets built to serve native load but that are also available to support third-party coordination sales. In addition, AEP argues that these principles underlie the installed capacity model that the Commission approved for PJM (the Reliability Pricing Model (RPM)). AEP notes that the RPM provides for participating load-serving entities to pay capacity charges regardless of the original purpose for which the generation was constructed.

35. AEP argues that the Commission does not quantify the general RTO benefits that AEP's native load and in-zone transmission customers allegedly receive by participating in PJM. AEP goes on to argue that even if it has enjoyed annual production cost savings or increased system sales profits, that has no bearing on the justness and reasonableness of rates for transmission service. AEP argues that to the extent that increased region-wide production cost savings matter, the January 31 Order never explained why those very benefits do not support the move away from license plate rates in favor of a single, region-wide rate. By definition, according to AEP, every dollar that AEP earned by selling energy in the region corresponds with dollar savings by purchasers in the region, or the sales would not have been made in the first place. AEP claims that the Commission failed to address this and other similar evidence, as well as evidence

confirming that these regional benefits could not have been obtained absent the region's heavy reliance on AEP's backbone EHV system.

36. AEP also argues that the January 31 Order failed to analyze the technical testimony provided by Mr. Pasternack. AEP asserts that this testimony suggests that AEP's extra high voltage facilities serve as the backbone of the regional grid and that without the existing AEP extra high voltage system, future PJM and Midwest ISO regional planning will be more difficult.

37. AEP argues that in focusing on the distinction between existing and new facilities and emphasizing the original purpose of the facilities, the Commission failed to address AEP's claim that depreciation is the ratemaking tool that accounts for changing uses of utility assets. AEP states that it submitted testimony showing that the current annual revenue requirement for AEP's 765 kV facilities is about \$220 million, whereas that figure would be approximately \$1.4 billion if those facilities were built in today's dollars. AEP asserts that the Commission did not address this point or articulate a reason why it was not relevant.³⁵

38. AEP disputes the Commission's rationale for rejecting AEP's argument that reallocating cost of existing facilities does not promote the goal of increasing investment. AEP argues that allocating the cost of existing facilities is not about promoting efficiency. Instead, AEP asserts that ratemaking precedent makes clear that allocating costs of existing facilities is about fairness, as the goal is to appropriately assign cost responsibility for facilities that already have been built. The only relevant efficiency question, according to AEP, is whether AEP's proposed cost allocation, which attempts to account for regional uses and benefits, would serve as a disincentive to new investment. AEP states that there is no evidence in the record to suggest that is the case.

39. AEP argues that the Commission already addressed questions of economic efficiency when it eliminated through-and-out charges that it perceived might restrict the dispatch of the lowest-cost efficient generators. AEP asserts that having changed the rules of pricing through-and-out service for efficiency purposes, the Commission's charge here was to implement a rate design that would account for the new rate paradigm for through-and-out service by adopting an alternate methodology to fairly allocate costs among through-and-out service customers. According to AEP, allowing through-and-out service customers a free ride while other native load customers subsidize their uses cannot be justified in the name of efficiency.

³⁵ AEP Rehearing Request at 16-17.

3. Commission Determination

40. We deny AEP's request for rehearing of the Commission's finding that the differences between new and existing facilities warrant that they be treated differently. We also note that AEP raises on rehearing the same arguments on this issue that it made in its complaint and that the Commission rejected in the January 31 Order.³⁶

41. We disagree with AEP's argument that the distinction between new and old facilities is not relevant to cost allocation issues. Within the context of RTOs, examining the original basis for making an investment is a reasonable component of a rate design analysis. In particular, the Commission explained the importance of regional planning process in making the distinction between old and new facilities:

Significantly, Midwest ISO and PJM plan the construction of new facilities based on each RTO's independent planning process, which helps to ensure that new projects are necessary to meet the reliability and economic needs of each RTO's system as a whole. Stakeholders in each RTO can participate in the RTO's regional planning process and, thus, can be part of the discussion that leads to the decision to build new facilities in which they will share the cost. Similarly, new cross-border facilities are planned pursuant to a joint RTO planning process under the [JOA]. In contrast, decisions to build existing facilities were not made as part of any regional planning process.^[37]

42. As the Commission also explained, while AEP's existing facilities were likely not planned in isolation, there is no evidence in the record to show that they were planned to address regional needs of either the Midwest ISO or PJM wholesale market, and therefore they are not comparable to new facilities that were planned pursuant to each RTO's regional planning process.³⁸ The existing facilities within each RTO were created principally to serve the customers of the transmission owners on whose system they are located and were not the product of centralized regional planning. Furthermore, AEP

³⁶ January 31 Order, 122 FERC ¶ 61,083 at P 128-34.

³⁷ *Id.* P 96 (internal footnotes omitted).

³⁸ *Id.* P 98.

undertook financial responsibility for the existing projects they planned before it was known whether any cost sharing policy would be adopted.³⁹

43. Contrary to AEP's assertions, the Commission did not disregard region-specific factors in concluding that the existing rate design had not been shown to be unjust and unreasonable. In that regard, the Commission did not, as AEP alleges, dismiss out of hand, and in fact explicitly acknowledged, that some of AEP's existing facilities provide benefits to customers outside the AEP zone.⁴⁰ However, although AEP claims that it derives less benefit from the facilities of all other transmission owners in both RTOs than those other transmission owners in both RTOs derive from AEP's existing facilities, the Commission noted that AEP "did not attempt to show the extent to which each specific customer within the region used and benefited from individual backbone facilities" because "[t]hat would have been a futile exercise."⁴¹ The Commission also explained that even though existing facilities may be part of an integrated transmission system, that alone is insufficient to find an existing rate design unjust and unreasonable.⁴²

44. We also reject AEP's suggestion that the current license plate rate design for existing facilities can only be just and reasonable if all members of the RTOs receive the same reciprocal benefits from using each others' systems. In deciding whether to join an RTO, a vertically integrated utility has to evaluate the benefits of joining the RTO against the possible costs, such as loss of transmission revenue from the elimination of through-and-out rates and the potential continuation of license plate rates. A utility that joins an RTO receives both quantifiable and non-quantifiable benefits, such as annual production cost savings, increased power sales profits through more efficient access to a much larger geographic area, improved system reliability, and construction incentives. As the Commission noted in the January 31 Order, AEP stated in its complaint that high-voltage transmission facilities in each RTO enable bulk transfers of lower-cost power to displace higher cost generating resources throughout the region and thus provide lower energy costs for customer throughout Midwest ISO and PJM. AEP did not provide persuasive evidence that it does not also enjoy these same benefits through its access as a member of PJM to the transmission facilities of all other Midwest ISO and PJM TOs at non-pancaked rates.⁴³

³⁹ *Pub. Serv. Comm'n of Wisc.*, slip op. at 15-16.

⁴⁰ January 31 Order, 122 FERC ¶ 61,083 at P 133.

⁴¹ *Id.* P 130 (*citing* AEP Complaint at 20).

⁴² *Id.* P 132.

⁴³ *Id.* P 150.

45. While we acknowledge that AEP's facilities may provide benefits to the region, we disagree with AEP's assertion that the benefits AEP *receives* from the region should have no bearing on the Commission's analysis of the existing rate design. All of the assets contributed to the RTO are part of the integrated grid, and the contribution of each transmission owner is necessary to produce the benefits. Thus, the Commission correctly considered the distinction between old and new facilities as one factor in determining that the costs of existing facilities, which were not built under a regional planning process, should not be charged to customers of utilities who played no role in the planning process, especially when the alleged use by those customers cannot be specifically proven.⁴⁴

46. We also reject AEP's assertion that the Commission failed to analyze the testimony provided by Mr. Pasternack. As the Commission explained, Mr. Pasternack himself acknowledged that AEP's existing facilities were not planned or built for regional use:

As Mr. Pasternack states, “[t]he most significant conclusion emerging from these [planning] studies was the finding that further development of the 345 kV and above transmission system would be required to meet the needs of the AEP region by 1990” and that “[b]ased on extensive analysis and evaluation, it was determined that the deployment of 765 kV transmission would provide the necessary transmission capability at lower cost and with less environmental impact.”⁴⁵ There is no specific evidence that third-party transmission usage played a role in the planning of or in the decision to build any of AEP's existing high-voltage facilities.^[46]

47. In fact, any facilities that are not approved by PJM in the PJM RTEP planning process must be funded locally and do not qualify for cost reallocation across PJM, let alone across the entire Midwest ISO/PJM region. If the costs of a new project are to be allocated to all customers across a region, the regional planning process helps to ensure that such new project is necessary to meet the reliability and economic needs of the region. Similarly, in Order No. 890, the Commission found that a new test that it adopted for determining transmission credits should not apply to existing facilities

⁴⁴ *Id.* P 131.

⁴⁵ AEP Complaint, Ex. AEP-300 at 10.

⁴⁶ January 31 Order, 122 FERC ¶ 61,083 at P 101.

because these were not subject to the increased planning and coordination requirements of Order No. 890.⁴⁷

48. To the extent we did not address AEP's depreciation argument in the January 31 Order, we do so here. We reject AEP's argument that we should consider the depreciation methodology in this proceeding because we are not discussing the vintage of AEP's transmission facilities. That the Commission did not specifically address AEP's arguments on depreciation in the January 31 Order does not invalidate the finding that it is reasonable for the RTOs to maintain different rate treatment for new and existing facilities. As the Commission explained in detail in the January 31 Order, the Commission based its finding that the existing rate design continues to be just and reasonable on the fundamental differences between new and existing facilities. While the costs for existing facilities that AEP wants to spread to all Midwest ISO and PJM customers are lower today than they were when the facilities were built as a result of depreciation, this is not a sufficient basis for us to find that the existing rate is unjust and unreasonable. The relevant evidence for purposes of finding the existing rate is still just and reasonable is that which sheds light upon the construction purpose of AEP's existing transmission facilities. As was explained in AEP's testimony, these facilities were constructed in the 1960s for the benefit of the customers of the individual transmission systems and did not result from a system-wide planning process. Hence, the depreciation argument made by AEP is irrelevant in this proceeding.

49. We further disagree with AEP's assertion that the Commission inappropriately considered the efficiency implications of the existing rate design. As part of its finding that the existing rate design continues to be just and reasonable, the Commission explained that unlike existing facilities, the rate design for new facilities has direct efficiency implications. As the Commission also explained in Order No. 890, rate design for new facilities is important because it provides incentives for construction, and adopting the correct rate design needs to provide sufficient certainty, without litigation delays, so that developers can obtain financing and projects can be constructed.⁴⁸ The Commission is obligated under the recently enacted section 219 of the FPA to "promote reliable and economically efficient transmission and generation of electricity by promoting capital investment in the enlargement, improvement, maintenance, and operation of all facilities for the transmission of electric energy in interstate commerce."⁴⁹

⁴⁷ *Preventing Undue Discrimination and Preference in Transmission Service*, Order No. 890, FERC Stats. & Regs. ¶ 31,241 at P 758, *order on reh'g*, Order No. 890-A, FERC Stats. & Regs. ¶ 31,261 (2007), *order on reh'g*, Order No. 890-B, 73 Fed. Reg. 39,092 (July 8, 2008), 123 FERC ¶ 61,299 (2008).

⁴⁸ Order No. 890, FERC Stats. & Regs. ¶ 31,241 at P 559-61.

⁴⁹ 16 U.S.C. § 824s (2006).

Thus it was appropriate for the Commission to note that maintaining the current license plate rate design to recover the cost of existing facilities would not have efficiency implications, and it was reasonable for the Commission to consider that fact as part of its determination that the existing rate design continues to be just and reasonable.

C. Cost Shifts

1. January 31 Order

50. With regard to the principles of cost causation for existing facilities, the Commission noted in the January 31 Order that these transmission facilities were developed by the individual transmission owners to benefit their own systems and their own customers, and that the license-plate rate design for these facilities was consistent with the principles of cost causation. Therefore, the Commission reasoned that it was appropriate to continue to allocate the cost of these facilities to the customers for whom the facilities were constructed and continue to serve. The Commission also recognized the effect of reallocating the costs of existing transmission facilities. The Commission stated in the January 31 Order that the record of the proceeding showed that replacing the license-plate rate design for existing facilities with any of the approaches advanced at the hearings would result in large and unacceptable cost shifts among the transmission owners.

51. The Commission considered a number of facts in reaching its conclusion that AEP had not established that the existing rate design was unjust and unreasonable, including that: (1) AEP's existing facilities were constructed for the benefit of the customers of the individual transmission systems and did not result from a system-wide planning process; (2) each of the proposed alternative rate designs found to be just and reasonable in the underlying initial decision presented unacceptable cost shifts; and (3) substantial shifts in cost responsibility could destabilize an RTO. Accordingly, the Commission found that the evidentiary record did not establish that the existing rate design was unjust and unreasonable and that the record did not present just and reasonable alternatives.

2. Rehearing Request

52. On rehearing, AEP argues that the Commission's cost shift analysis is flawed because the Commission rejected AEP's position that any cost-shift analysis should account for the level of costs previously allocated under through-and-out rates. AEP disputes one basis for this finding, which is that termination of Seams Elimination Cost Adjustment without a long-term replacement rate in place signifies that the Commission did not intend to implement a lost revenues mechanism. AEP states that it has never argued for a long-term lost revenues rate design, but that it is proposing a straightforward cost allocation based on current peak usage of the grid.

53. In addition, AEP argues that the Commission in the January 31 Order misconstrued the nature of the cost-shift concerns that the Commission expressed in prior orders. AEP notes that the Commission has previously expressed concern about cost shifts resulting from loss of through-and-out revenue and stressed that the end state should be a single, system-wide average rate which reflects the regional nature of the service provided.

54. AEP also argues that the cost-shift analysis adopted in Opinion No. 494 and followed in the January 31 Order creates an internal inconsistency in the *Going Forward Principles*⁵⁰ that renders them virtually meaningless. AEP cites the preamble to Principle 11 of the *Going Forward Principles*, which states:

Where transmission owners have turned over operational or functional control over their facilities to PJM or [Midwest ISO], it would be unfair if that decision caused unreasonable economic harm to such transmission owners or the load serving entities and end-use customers within or to be included within PJM or [Midwest ISO]. *Economic harm would include undue reductions in transmission revenue and/or cost shifts.*^{51]}

AEP states that if the “economic harm” incurred as a result of “reductions in transmission revenue” could be remedied only by avoiding cost shifts measured from a starting point that assumed that the parties already agreed to such “reductions in transmission revenue,” then the provision collapses of its own weight.⁵² AEP asserts that the Commission consistently has held that contracts and settlements such as the *Going Forward Principles* must be interpreted to give meaning to all their provisions so as not to render certain provisions superfluous. According to AEP, the Commission’s current cost shift analysis leads to an interpretation of the *Going Forward Principles* that fails to meet this standard.

⁵⁰ The *Going Forward Principles and Procedures* is an agreement that established principles and procedures to guide Midwest ISO and PJM markets participants in the development of a long-term transmission pricing structure. The *Going Forward Principles* were submitted to the Commission in a report from the Commission’s Chief Administrative Law Judge, *Midwest Indep. Transmission Sys. Operator, Inc.*, 106 FERC ¶ 61,024 (2004), and subsequently accepted by the Commission, *Midwest Indep. Transmission Sys. Operator, Inc.*, 106 FERC ¶ 61,262 (2004).

⁵¹ AEP Rehearing Request at 24 (emphasis added by AEP).

⁵² *Id.* at 25.

55. AEP argues that, with respect to the “abruptness” of the cost shifts resulting from the elimination of through-and-out charges, prior rulings make clear that the Commission’s focus was on the fact that the task of developing a consensus long-term transmission pricing structure would not be easy and that some mechanism was needed to cover the period during which the parties were developing the long-term solution. AEP asserts that, contrary to the suggestion in the January 31 Order, the Commission’s prior rulings make clear that the concerns were always about addressing cost shifts and that those concerns extended beyond the close of the transition period. AEP contends that there would otherwise have been no basis for implementing Seams Elimination Cost Adjustment in the first place, because each of the policy grounds announced in Opinion No. 494 and adopted in the January 31 Order applied with equal force during the transition period: the existing facilities were built primarily to serve native load and outside an RTO-like planning process, and a majority of PJM and Midwest ISO participants opposed Seams Elimination Cost Adjustment.

56. AEP asserts that the cost shift concerns that were present on March 31, 2006 (when Seams Elimination Cost Adjustment payments terminated) were just as present on April 1, 2006, and also on February 1, 2008 (when the Independent RTO Pricing Design proposal became effective). According to AEP, if the Commission relies upon the transitional Seams Elimination Cost Adjustment to defend the current license plate structure, then the Commission is in effect arguing that unjust and unreasonable rates can be tolerated as long as they are not put into effect “abruptly.” AEP contends that an attempt to support the cost-shift analysis in the January 31 Order on this basis, by pointing to the fact that the Commission allowed the Seams Elimination Cost Adjustment payments to expire without having put in place a replacement rate, is not reasoned decision making.

3. Commission Determination

57. We reject AEP’s arguments. AEP raises no cost shift argument on rehearing not already addressed by the Commission in the January 31 Order.⁵³ AEP’s argument is essentially that the Commission should find that the continuation of unpancaked license plate rates is unjust and unreasonable because of the cost shift that occurred when the Commission eliminated pancaked rates between Midwest ISO and PJM. As the Commission stated in the January 31 Order, “The cost shift that occurred when the prior rate changed to the existing rate (and that, in any event, the Commission already addressed) is not a sufficient basis to find that the existing rate is unjust and unreasonable.”⁵⁴

⁵³ January 31 Order, 122 FERC ¶ 61,083 at P 114-22.

⁵⁴ *Id.* P 122.

58. We reject AEP's argument that the Commission rendered Principle 11 of the *Going Forward Principles* meaningless by finding that the cost shift related to the revenue AEP lost with the elimination inter-RTO rate pancaking was not a valid basis upon which to find the existing license plate rates unjust and unreasonable. Principle 11 states in part that it would be unfair if a transmission owner's decision to join Midwest ISO or PJM caused unreasonable "economic harm", and defines "economic harm" to include reduced transmission revenue and/or cost shifts.⁵⁵ The Commission has consistently recognized that the immediate elimination of pancaked license-plate inter-

⁵⁵ Principle 11 of the *Going Forward Principles* states:

Where transmission owners have turned over operational or functional control over their facilities to PJM or [Midwest ISO], it would be unfair if that decision caused unreasonable economic harm to such transmission owners or the load serving entities and end-use customers within or to be included within PJM or [Midwest ISO]. Economic harm would include undue reductions in transmission revenue and/or cost shifts. This principle should be recognized as part of a long-term transmission pricing structure. A long-term transmission pricing structure that would result in material reductions in transmission revenues or costs shifts could allow for the possibility of a reasonable phase-in of such pricing structure. When fully implemented, the long-term transmission pricing structure will apply throughout the Combined Region. The long-term transmission pricing structure must meet the "just and reasonable" standard, allowing transmission owners an opportunity to recover their costs, including a fair return on investment, and the other standards of the FPA. An important factor in determining whether these standards have been met in any long-term transmission pricing structure is the degree to which cost responsibility for facilities is assigned to those who use or benefit from such facilities, regardless of whether those users or beneficiaries are located inside or outside the transmission owner's footprint. If the Commission requires a long-term pricing structure to be implemented or phased-in throughout the Combined Region, the implementing rate design within an RTO may not preclude achieving the economic objectives of such long-term transmission pricing structure within the Combined Region, as well as within the RTO.

RTO rates would cause a cost shift and adopted the Seams Elimination Cost Adjustment transition mechanism to mitigate that immediate shift. For instance, the Commission explained when it adopted the Seams Elimination Cost Adjustment that “in order to mitigate abrupt shifts of the portion of the transmission revenue requirement that previously was recovered from through and out service customers under pancaked rates to customers within the license plate pricing zone, the Commission has approved the use of transitional rate mechanisms providing for recovery of revenues lost due to the elimination of rate pancaking for a short period upon the adoption of license plate rates.”⁵⁶

59. Under AEP’s flawed interpretation of Principle 11, however, the general guidance relating to unreasonable economic harm being unfair is inappropriately construed to mean that parties to the *Going Forward Principles* were agreeing that the RTOs could not propose to continue using the license plate rate design after the Seams Elimination Cost Adjustment payment expired because the cost shift that occurred when the Commission eliminated inter-RTO rate pancaking caused unreasonable economic harm. This interpretation is in direct conflict with the Commission’s explicit finding in the November 2004 Order, which was issued after the *Going Forward Principles* were accepted in March 2004, that the required reevaluation of the fixed cost recovery policies for pricing transmission service between the two RTOs was *not* a mandate that license plate rates for service between must be eliminated at the end of the term.⁵⁷

60. We also disagree with AEP that by citing the transitional nature of the Seams Elimination Cost Adjustment, the Commission was arguing that unjust and unreasonable rates can be tolerated as long as they are not put into effect abruptly.⁵⁸ Specifically, the Commission noted in the January 31 Order that had it meant to require the RTOs to eliminate license plate rates, then the temporary, transitional nature of the Seams Elimination Cost Adjustment mechanism would be meaningless.⁵⁹

61. AEP’s argument that the transitional nature of the Seams Elimination Cost Adjustment is irrelevant is based on AEP’s incorrect belief the Commission, by recognizing the cost shift that would occur with the elimination of pancaked inter-RTO rates, was finding that the license plate rate design without the Seams Elimination Cost

⁵⁶ *Midwest Indep. Transmission Sys. Operator, Inc.*, 109 FERC ¶ 61,168, at P 57 (2004).

⁵⁷ *Id.* P 62.

⁵⁸ AEP Rehearing Request at 26-27.

⁵⁹ January 31 Order, 122 FERC ¶ 61,083 at P 118.

Adjustment was unjust and unreasonable – something the Commission explicitly did not do. If, as AEP suggests, the purpose of the Seams Elimination Cost Adjustment was to make an otherwise unjust and unreasonable license plate rate design just and reasonable until a different rate design took effect, then the Commission would not have allowed the Seams Elimination Cost Adjustment to expire in March 2006, prior to the end of the initial transition period on February 1, 2008.⁶⁰

62. Furthermore, as the Commission noted in the January 31 Order, only one transmission owner supports AEP's complaint, and that transmission owner only supported AEP's proposal in part.⁶¹ As the Commission also explained in Opinion 494-A,⁶² although majority support was only one aspect of the analysis, and not uniquely critical to the Commission's decision, the positions of regional participants are indeed relevant. Unlike holding companies and other individually-owned utilities, where allocation of sunk costs has little or no efficiency effects, RTOs are voluntary agreements of transmission owners, and cost allocations may have significant effects on transmission owner decisions to join or remain in the RTO. Because of the ongoing incentive effects of cost reallocation, we cannot find that the transmission owners' agreement for joint management of their facilities automatically renders the pre-existing basis upon which transmission owners joined the RTO unjust and unreasonable, particularly (but not solely) given the opposition of the majority of the transmission owners.⁶³

D. Cost Allocation

1. January 31 Order

63. In the January 31 Order, the Commission found that the existing inter-RTO rate design fairly allocates transmission costs to those who benefit from the facilities in the combined Midwest ISO/PJM region, in accordance with cost causation principles.⁶⁴

⁶⁰ *Id.*

⁶¹ *Id.* P 121.

⁶² Opinion No. 494-A, 122 FERC ¶ 61,082 at P 38.

⁶³ *See also Pub. Serv. Comm'n of Wisc.*, slip op. at 10-12 (finding that the Commission may give weight to a proposal with majority support in an RTO as long as it makes an independent finding of the reasonableness of the rates).

⁶⁴ January 31 Order, 122 FERC ¶ 61,083 at P 165.

2. Request for Rehearing

64. AEP argues that the January 31 Order is inconsistent with cost causation principles because the Commission did not consider the benefits of AEP's system enjoyed by non-native load customers. Citing *California Power Exchange Corp.*⁶⁵ and *Midwest ISO Transmission Owners v. FERC*,⁶⁶ AEP asserts that cost causation precedent requires that costs be allocated based on benefits to customers and cost incurrence. AEP also argues that the Commission failed to distinguish *KN Energy, Inc. v. FERC*⁶⁷ from this proceeding. In *KN Energy*, the court held that the Commission could depart from traditional cost causation principles in order to allocate take-or-pay costs to all open access transportation customers, even though the pipelines had originally entered into the take-or-pay contracts in order to serve its bundled sales customers. Among other things, the court upheld the Commission's reasoning that while the transportation customers may not have directly caused the take-or-pay costs, all segments of the industry benefit from the move to open access transportation.

65. AEP also argues that the Commission failed to apply the standard established in the *Going Forward Principles*. AEP states that in that settlement, a majority of Midwest ISO and PJM participants agreed that a just and reasonable long-term pricing structure would assign cost responsibility for facilities to those who use or benefit from those facilities, regardless of whether they are located inside or outside the transmission owner's footprint. AEP asserts that the Commission failed to address and explain its departure from the *Going Forward Principles* in both the January 31 Order and Opinion Nos. 494 and 494-A.

⁶⁵ 106 FERC ¶ 61,196 at P 17 (2004).

⁶⁶ 373 F.3d 1361, 1368 (D.C. Cir 2004).

⁶⁷ 968 F.2d 1295 (D.C. Cir. 1992) (*KN Energy*). *KN Energy* involved the take-or-pay problems that arose from clauses in gas purchase contracts between pipelines purchasing gas and the producers of that gas. These clauses required pipelines to either purchase a specified percentage of the producer's deliverable gas or to make prepayments for that percentage even if it was not purchased. Between 1977 and 1982, pipelines undertook take-or-pay contracts at prices above then-current market levels, anticipating that the cost of gas would rise. This anticipation proved wrong and pipelines committed themselves to prices well in excess of what the market actually required, resulting in a sunk cost for the pipeline industry of several billion dollars. *KN Energy*, 968 F.2d 1295 at 1297. Further, the contract clauses committed the pipelines to purchase gas in excess of their needs because customers reduced purchases from the pipeline when they availed themselves of unbundled transportation service.

3. Commission Determination

66. We reject AEP's argument that the January 31 Order is inconsistent with cost causation principles and deny rehearing on this issue. AEP cites a number of cases that are not applicable here because these cases do not involve cost allocation for pre-existing transmission facilities of utilities that joined an RTO. Therefore, our determination to permit the continuation of a license plate rate design is not inconsistent with these decisions.⁶⁸ In *California Power Exchange Corp.*, the costs involved were legal expenses incurred in seeking recovery of a performance bond, and the Commission provided that recovery of these costs reasonably could be imposed on the defaulting party, which had a legal obligation to pay for legal expenses. *Midwest ISO Transmission Owners v. FERC* involved the allocation of Midwest ISO's ongoing management costs; the ISOs and RTOs must allocate such management costs to participants. Midwest ISO's operating costs are incurred to serve all customers across its region, in contrast to the costs of AEP's existing facilities, which were incurred to serve local load. Therefore, a determination that the ISO's management costs should be shared by participants does not establish that the same result must necessarily apply to the rate-based pre-existing transmission facilities built by transmission owners prior to their entry into the RTO.

67. *KN Energy* is also not applicable because the costs involved in that case, take-or-pay costs arising from clauses in gas purchase contracts, are distinct from the costs involved here. In *KN Energy*, the court specifically found that it was acceptable for the cost of take-or-pay losses to be spread to *all* segments of the natural gas industry benefitting from open access transportation, but that such allocation was not required.⁶⁹ The court also pointed out that pipeline restructuring, which caused the take-or-pay crisis, benefited all actors except fuel-switchable users.⁷⁰ On the other hand, as we have repeatedly found, while AEP's existing facilities were likely not planned in isolation, there is no evidence in the record to show that they were planned to address regional needs of either the Midwest ISO or PJM wholesale market. The existing facilities within each RTO were created principally to serve the customers of the transmission owners on whose system they are located and were not the product of central planning, and therefore the costs of these facilities were not undertaken for the benefit of all participants in the combined Midwest ISO/PJM region.

⁶⁸ Opinion No. 494-A, 122 FERC ¶ 61,082 at P 39.

⁶⁹ *KN Energy*, 968 F.2d 1295 at 1302.

⁷⁰ *Id.* (“[T]he benefit principle may only ask us to look at a host of contributing causes for the cost incurred (as ascertained by a review of those who benefit from the incurrence of the cost) and assign them liability too.”).

68. We also reject AEP's assertion that we failed to apply the standard established in the *Going Forward Principles* settlement in the January 31 Order. Under the cost causation principle, upon which the *Going Forward Principles* are based, a long-term pricing structure would assign cost responsibility for facilities to those who use or benefit from those facilities. As explained above, the January 31 Order does not represent a departure from cost causation because we specifically find that the costs of AEP's existing facilities were not undertaken under a regional planning process or for the benefit of all participants in the combined Midwest ISO/PJM region.

E. Lost Through-and-Out Revenue

1. January 31 Order

69. In the January 31 Order, the Commission found that AEP's lost through-and-out revenue is not a sufficient basis to find that the existing inter-RTO rate design is unjust and unreasonable.⁷¹ The Commission stated that through-and-out rates are antithetical to the efficient dispatch of a system because they raise barriers to regional scheduling, and that AEP and other RTO members should have been on notice that pancaked rates would be eliminated.⁷² The Commission also noted that while it did provide interim recovery of lost through-and-out revenue through the Seams Elimination Cost Adjustment transition rate mechanism, it never stated that those lost revenues would continue to be recovered on a permanent basis.⁷³ The Commission also repeated its finding in Opinion No. 494 that the continued use of license-plate rates for existing facilities is not related to the recovery of lost through-and-out revenues.⁷⁴

2. Rehearing Request

70. AEP argues that the Commission creates a strawman by claiming that AEP should have been on notice that pancaked rates would be eliminated at some point after AEP joined PJM and, therefore, that AEP has no claim to a permanent entitlement to lost revenues. AEP states that it never disputed that the Commission's goal was to eliminate pancaked rates, and that it has never argued for a permanent lost-revenue mechanism. Rather, AEP states that it has consistently argued that if the Commission chose to do away with the cost-allocation function served by through-and-out charges, it must adopt

⁷¹ January 31 Order, 122 FERC ¶ 61,083 at P 105.

⁷² *Id.* P 111.

⁷³ *Id.*

⁷⁴ *Id.* P 112.

another mechanism to fairly allocate costs to third parties, because third-party use of AEP's facilities would not end when transaction-based charges ended.

71. AEP argues that the Commission cites only Opinion No. 494, which was issued in 2007, to support the finding in the January 31 Order that AEP should have evaluated the benefits of joining the RTO against the possible loss of transmission revenue from the elimination of through-and-out rates. AEP contends that the Commission is suggesting that AEP should have known as far back as 2002 that its customers would be asked to subsidize hundreds of millions of dollars worth of transmission use by others in return for receiving generalized and unquantifiable RTO benefits, based on a rationale that would first be adopted in 2007 in Opinion No. 494.

72. AEP claims that the Commission also misread its own precedent, as the "trade-off" between the loss of through-and-out revenue and RTO benefits was never the basis of the Commission's elimination of through-and-out rates. AEP argues that the Commission recognized that license plate rates without a pancaked rate element (i.e., through-and-out charges) raised cost shift concerns for companies like AEP, whose systems were heavily used.

73. AEP argues that from the outset, the debate was never about whether or not transmission owners should be compensated by those who use and benefit from the owners' assets because, according to AEP, they clearly should be. Instead, AEP asserts that the only issue was whether the transactional nature of through-and-out charges could skew energy prices. Thus, in each order prior to Opinion No. 494, AEP states that the Commission's only caveat was that "rates to recover embedded costs must be redesigned carefully to avoid such effects."⁷⁵ AEP also argues that the Commission looks back to the period when many of AEP's extra high voltage facilities were first built, but then jumps over the substantial historical uses of these facilities made by customers throughout what is now the combined Midwest ISO/PJM region. In that respect, AEP argues that the Commission seeks to have it both ways – the Commission first eliminates transaction-specific charges because they act as a toll on the region's use of AEP's essential extra high voltage facilities and then argues that no replacement charge mechanism is appropriate because these same essential extra high voltage facilities were not planned and built for regional uses.

74. AEP argues that contrary to the Commission's assertion in the January 31 Order, the Commission precedent addressing the elimination of through-and-out charges in the combined Midwest ISO/PJM region has consistently recognized AEP's cost causation and cost shifting concerns and repeatedly charged the stakeholders to develop a long-term

⁷⁵ AEP Rehearing Request at 23 (*citing Ameren Services Co.*, 105 FERC ¶ 61,216, at P 41 (2003)).

transmission pricing structure that would fairly account for the regional uses of the grid, as provided for under the Commission-approved *Going Forward Principles and Procedures (Going Forward Principles)* settlement. AEP asserts that none of these cases can be read to suggest that the Commission believed (and that AEP should have understood) that these cost shift concerns would be offset by unspecified generalized RTO benefits. AEP contends that the Commission's misreading of its prior orders undermines its ability to "articulate... a rational explanation for its action" because "reasoned decision-making necessarily requires consideration of relevant precedent."⁷⁶

3. Commission Determination

75. We deny AEP's request for rehearing and find that the Commission did not "misstate" history nor did it "misread" its own precedent in the January 31 Order. The Commission understood and acknowledged, as it has done in various proceedings, the concerns about RTOs continuing to use a license-plate rate design. It is those concerns that led the Commission to require, in Order No. 2000 for RTOs in general and in the proceedings eliminating through-and-out rates between Midwest ISO and PJM specifically, that RTOs submit for Commission consideration a reevaluation of the license plate rate design after an initial period. However, in all cases, the Commission was unambiguous: the reevaluation was not a mandate to either continue or abandon license plate rates. AEP's argument appears to be that because the Commission recognized that there are concerns with continuing license plate rates, the Commission always intended to use the required reevaluation to eliminate them. That is simply not the case.

76. The Commission has stated in the past, and we acknowledge here, that there are legitimate concerns about the continuation of license-plate rates in Midwest ISO and PJM. That does not lead to the inexorable conclusion that in the context of RTOs, the current license plate rate design for existing facilities is unjust and unreasonable. There are legitimate and counterbalancing concerns about either maintaining or eliminating license-plate rates. As the Commission explained:

In addressing transmission rate design within and between RTOs, the Commission sought to craft a reasonable balance among a number of interrelated factors including: the original basis for constructing facilities, the effect of the RTOs' planning process on the decision to construct, the nature of the agreements by [transmission owners] to form RTOs, the cost impacts of the various rate designs, the uses of

⁷⁶ *Id.* (citing *Williams Gas Processing-Gulf Coast Co. v. FERC*, 475 F.3d 319, 326 (D.C. Cir. 2006) (citations omitted)).

the transmission system, and the need for new infrastructure within the RTO regions. Accordingly, the Commission has permitted different just and reasonable rate designs reflective of particular system characteristics and stakeholder input.^[77]

77. AEP raises no arguments on rehearing that the Commission did not already consider in finding that license plate rates continue to be just and reasonable. AEP believes that its concerns about maintaining a license plate rate design outweigh the Commission's and other parties' concerns about abandoning license plate rates. But nothing in AEP's recitation in its request for rehearing of the same arguments it already made persuades us to arrive at a different conclusion. We once again note that, as the courts have found, rate design "is less a science than it is an art."⁷⁸ In particular, "[a]llocation of costs is not a matter for the slide-rule. It involves judgment on a myriad of facts. It has no claim to an exact science."⁷⁹

78. AEP is also incorrect that the Commission is attempting to have it both ways by eliminating pancaked rates but then not providing a permanent replacement charge mechanism. This argument is based on the false premise that the unpancaked license plate rate design is necessarily unjust and unreasonable without a permanent lost revenue mechanism. However, AEP itself argues that it is not advocating a long-term lost revenues rate design but instead "proposes a straight forward cost allocation based on current peak usage of the grid."⁸⁰ Similarly, the Commission did not find that a long-term lost revenue mechanism is needed for the existing rates to continue to be just and reasonable. AEP may believe that its cost allocation proposal is just and reasonable, but as the Commission explained in the January 31 Order, the fact that there may be alternate rate designs that are *also* just and reasonable does not mean that the Commission must reject the existing inter-RTO rate design.⁸¹

⁷⁷ January 31 Order, 122 FERC ¶ 61,083 at P 83.

⁷⁸ *Cities of Bethany, et al. v. FERC*, 727 F.2d 1131, 1138 (D.C. Cir. 1984); *Ala. Elec. Coop., Inc. v. FERC*, 684 F.2d 20, 27 (D.C. Cir. 1982).

⁷⁹ *Colo. Interstate Gas Co. v. FPC*, 324 U.S. 581, 589 (1945) (*Colo. Interstate*).

⁸⁰ AEP Rehearing Request at 24.

⁸¹ January 31 Order, 122 FERC ¶ 61,083 at P 113.

F. AEP's Alternative Rate Proposal**1. January 31 Order**

79. In its Complaint, AEP proposed a replacement highway/byway rate design that provides for allocation of the costs of both existing and new high-voltage transmission facilities (those facilities operated at 345 kV and above) across the combined Midwest ISO/PJM region. AEP argued that under its proposal, all customers that benefit from the use of Midwest ISO and PJM backbone transmission facilities would share the burden of the costs. At the same time, AEP proposed to maintain the current allocation methodology for existing and new lower-voltage transmission facilities within the combined Midwest ISO/PJM region. Second, as an alternative, AEP proposed a rate design under which the costs of all facilities at 765 kV and above are spread across the entire combined Midwest ISO/PJM region. Third, in the event the Commission found AEP's alternative proposals not to be just and reasonable, AEP asked the Commission to initiate hearing procedures to determine what would be a just and reasonable rate design for transmission service in the combined Midwest ISO/PJM region.

80. In the January 31 Order, the Commission found that because AEP had not met its burden to demonstrate that the existing rate design was unjust and unreasonable, the Commission did not need to and would not decide whether AEP's proposed rate design is just and reasonable.⁸²

2. Request for Rehearing

81. On rehearing, AEP argues that the January 31 Order erroneously failed to address the rate proposal that AEP presented in its Complaint. AEP states that its rate design would ensure that the costs of existing extra high voltage facilities that integrate the Midwest ISO/PJM region are allocated among those who use and benefit from the facilities, including AEP's customers.

82. AEP takes issue with the January 31 Order's criticisms of AEP's proposal. AEP argues that the January 31 Order noted the absence of a single Midwest ISO/PJM joint dispatch and the presence of transmission constraints, but these considerations do not address the level to which customers in the region benefitted from AEP's extra high voltage network. AEP also asserts that the Commission erred in determining that the relationship between existing facilities and the Auction Revenue Rights to use those facilities is an impediment to adopting AEP's rate proposal for those existing facilities.

⁸² *Id.* P 149.

83. AEP asserts that even if certain customers faced increased transmission charges under its proposal, they would receive corresponding benefits from access to the entire regional transmission system without paying access charges. Access to lower-cost generators, according to AEP, has resulted and will result in lower average LMPs, enhanced reliability and lower generation reserve requirement costs.

3. Commission Determination

84. We deny rehearing on this issue. AEP cites to the January 31 Order's "criticisms" of its proposal. However, the Commission in the January 31 Order did not substantively assess AEP's alternative proposal. AEP erroneously refers to our discussion of the existing rate design and AEP's criticism of the existing rate design as criticisms of AEP's alternative proposal.⁸³

85. As discussed above, we reiterate our finding in the January 31 Order that AEP has failed to show that the existing rate design in the combined Midwest ISO/PJM area is unjust and unreasonable. Therefore, we need not decide whether AEP's proposed rate design is just and reasonable.

The Commission orders:

The request for rehearing of the January 31 Order is hereby denied, as discussed in the body of this order.

By the Commission. Commissioner Moeller not participating.

(S E A L)

Kimberly D. Bose,
Secretary.

⁸³ See, e.g., AEP Rehearing Request at 54 (*citing* January 31 Order, 122 FERC ¶ 61,083 at P 129 ("We therefore cannot find unjust and unreasonable the existing rate design...")).