

111 FERC ¶ 61,140
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Trans-Elect NTD Path 15, LLC

Docket No. ER05-17-001

ORDER DENYING REHEARING

(Issued May 4, 2005)

1. In an order issued on December 2, 2004, the Commission accepted for filing Trans-Elect NTD Path 15, LLC's (NTD Path 15) transmission revenue requirement and proposed Transmission Owner Tariff (TO Tariff) (Revenue Requirement and TO Tariff Filing), suspended it for a nominal period, to become effective upon commencement of commercial operation of the Path 15 Upgrade, subject to refund and subject to the outcome of the proceeding established in Docket No. PL05-5-000.¹ The Commission also established hearing and settlement judge procedures. In this order, we deny the requests for rehearing of the December 2 Order.

Background

2. California's Path 15 is a uniquely critical path with transmission limitations that have had serious impacts on the ability to move power over the system.² In May 2001, the Secretary of Energy authorized the Western Area Power Administration (Western) to explore ways to relieve California's Path 15 capacity constraints and increase reliability through transmission expansion in the Path 15 corridor. Through a competitive selection process, Western chose Trans-Elect Inc. (Trans-Elect) and Pacific Gas & Electric

¹ *Trans-Elect NTD Path 15, LLC*, 109 FERC ¶ 61,249 (2004) (December 2 Order).

² *Western Area Power Admin.*, 99 FERC ¶ 61,306 at 62,227 (June 12 Order), *reh'g denied*, 100 FERC ¶ 61,331 at P 7 and n.4 (2002).

Company (PG&E) to build an 83-mile, 500 kV transmission line within the existing Path 15 transmission corridor and make related modifications to PG&E's Los Banos and Gates substations (Path 15 Upgrade).³

3. On June 12, 2002, the Commission accepted a letter agreement (Letter Agreement) entered into by Western, Trans-Elect and PG&E (Path 15 Upgrade participants) which, among other things, set forth rate principles for the recovery of costs associated with the Path 15 Upgrade.⁴ On March 25, 2004, the Commission approved a settlement agreement between the California Public Utilities Commission (CPUC), Trans-Elect and NTD Path 15 addressing related issues (CPUC Settlement).⁵

4. In January 2003, Trans-Elect filed a letter of intent with the California Independent System Operator Corporation (CAISO) to become a Participating Transmission Owner (PTO) and turn over operational control of its rights in the Path 15 Upgrade to the CAISO. On October 14, 2003, pursuant to delegated authority, the Commission's Director of the Division of Tariffs and Market Development - West accepted the CAISO's amendment to its Transmission Control Agreement to include NTD Path 15 as a PTO.⁶

5. On June 30, 2004, the Commission accepted for filing the Coordinated Operations and Interconnection Agreement entered into by PG&E, NTD Path 15 and Western, to become effective July 1, 2004.⁷

6. On October 4, 2004, NTD Path 15 filed its Revenue Requirement and TO Tariff Filing. In the December 2 Order, the Commission accepted the filing, suspended it for a nominal period, to become effective upon commencement of commercial operation of the Path 15 Upgrade, subject to refund and subject to the outcome of the proceeding established in Docket No. PL05-5-000. The Commission also established hearing and

³ Once in service, the Path 15 Upgrade will increase transmission capacity from Southern to Northern California by 1,500 MW and from Northern to Southern California by 1,100 MW. Exhibit NTD-7 at 4:1-6.

⁴ June 12 Order, 99 FERC ¶ 61,306.

⁵ *Western Area Power Admin.*, 106 FERC ¶ 61,295 (2004).

⁶ *California Indep. Sys. Operator Corp.*, Letter Order, Docket No. ER03-1217-000 (Oct. 14, 2003).

⁷ *Pacific Gas & Elec. Co.*, 107 FERC ¶ 61,335 (2004).

settlement judge procedures. On December 22, 2004, the CAISO notified the Commission that the Path 15 Upgrade reached commercial operation effective on December 22, 2004.

7. The Transmission Agency of Northern California, the Cities of Santa Clara and Redding, California, and the M-S-R Public Power Agency (collectively, TANC) jointly and NTD Path 15 filed requests for rehearing of the December 2 Order. TANC filed an answer to NTD Path 15's request for rehearing.

Discussion

A. Procedural Matters

8. Rule 713(d)(1) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713(d)(1) (2004), prohibits answers to requests for rehearing. Accordingly, we will reject TANC's answer to NTD Path 15's request for rehearing.

B. Income Tax Allowance

9. In its Revenue Requirement and TO Tariff Filing, among other things, NTD Path 15 proposed a Base Case Revenue Requirement which includes an imputed tax allowance and retains a 13.5 percent return on common equity.⁸ In the alternative, NTD Path 15 proposed an Alternative Case Revenue Requirement which was essentially identical but eliminated the income tax allowance and increased the return on equity to approximately 22.78 percent to yield an equivalent revenue requirement, including an after-tax return on equity of 13.5 percent.⁹ Among other things, protestors challenged the inclusion of an income tax allowance in NTD Path 15's return on equity given the opinion of the United States Court of Appeals for the District of Columbia Circuit (D.C. Circuit) in *BP West Coast Products, LLC v. FERC*,¹⁰ finding that the Commission erred by including an income tax allowance in a limited partnership's cost of service computation because no income taxes had been or would be paid on that partnership's income.

⁸ December 2 Order, 109 FERC ¶ 61,249 at P 18.

⁹ *Id.*

¹⁰ *BP West Coast Products, LLC v. FERC*, 374 F.3d 1263 (*BP West*), *reh'g denied*, 2004 U.S. App. LEXIS 20796-98 (2004).

10. In the December 2 Order, the Commission allowed NTD Path 15 to include an income tax allowance associated with its 13.5 percent return on common equity for the first three years of operation in which the rates are fixed pursuant to an approved-rate moratorium, but the Commission made the income tax allowance subject to refund and subject to the outcome of the generic proceeding established in Docket No. PL05-5-000 to obtain public comments on the policy the Commission should adopt in light of *BP West*.¹¹ The Commission reached this determination based upon: (1) the circumstances of this proceeding, including that construction of the Path 15 Upgrade project had essentially been completed and that there was an agreed-upon rate structure that was relied upon to initially finance and construct the Path 15 Upgrade; (2) the critical need that the financial community have some certainty and assurance that initial ratemaking decisions made by the Commission, that enable financing packages to be completed, can be relied upon by all parties with respect to initial cost recovery in order to finance much needed electric infrastructure; and (3) the possibility that *BP West* and its application may represent a generic issue that must be viewed in the context of all of the industries that the Commission regulates.¹² The Commission also rejected the proposed Alternative Case Revenue Requirement¹³ and set other issues of material fact for hearing and settlement judge procedures.¹⁴

11. On rehearing of the December 2 Order, TANC challenges the Commission's determination that, at the time it accepted the Letter Agreement in 2002, it was not necessary for the Commission to explicitly state that it was providing an income tax allowance associated with the authorized return on common equity because Commission precedent was clear that a public utility would always receive an income tax allowance associated with its rate of return.¹⁵ TANC asserts that the Commission erred because the policy on income tax allowance was only applicable to public utilities making comprehensive rate filings, which include an income tax allowance calculation as part of

¹¹ December 2 Order, 109 FERC ¶ 61,249 at P 29.

¹² *Id.*

¹³ *Id.* at P 31 n.25.

¹⁴ *Id.* at P 30-32.

¹⁵ *Citing id.* at P 27.

the overall rate approved by the Commission,¹⁶ and that the Letter Agreement filed, which addressed return on equity, capital structure and depreciation life for the asset, was not such a comprehensive filing. TANC further contends that, by the time NTD Path 15 made its comprehensive filing in October 2004, NTD Path 15 could no longer reasonably rely on the Commission's tax allowance policy because, by then, all public utilities were on notice that the D.C. Circuit had remanded the tax policy to the Commission for further proceedings. TANC adds that NTD Path 15 never communicated to the Commission when it filed the Letter Agreement that investors relied upon the tax allowance as a component of the revenue requirement or that it planned to organize as a limited liability corporation.

12. We disagree. Irrespective of whether the Letter Agreement was a comprehensive filing or whether, at the time of the filing of the Letter Agreement, NTD Path 15 informed the Commission that it intended to organize as a limited liability corporation or that investors relied upon the income tax allowance as a component of the revenue requirement, at the time the Letter Agreement was filed and approved, a rate of return on equity would have included an associated income tax allowance for, among others, a limited liability corporation such as NTD Path 15. Since one of the rate principles accepted as part of the Letter Agreement was the rate of return on equity, it would have been reasonable for NTD Path 15 and investors to assume that the Commission-approved rate of return for the Path 15 Upgrade included an income tax allowance. TANC has failed to convince us otherwise; therefore, we deny this request for rehearing.

13. TANC also claims that the Commission erred by allowing NTD Path 15 to recover the income tax allowance, subject to refund, because, as a limited liability corporation, NTD Path 15 is not required to pay federal income taxes, and, thus, with the income tax allowance, it would recover an amount greater than its actual costs.¹⁷ In *BP West*, the D.C. Circuit remanded to the Commission its determination regarding the proper tax

¹⁶ Citing 18 C.F.R. § 35.12 (2004); *Metropolitan Edison Co.*, 44 FERC ¶ 61,053 at 61,146 (1988).

¹⁷ Citing *Regulations Implementing Tax Normalization for Certain Items Reflecting Timing Differences in the Recognition of Expenses or Revenues for Ratemaking and Income Tax Purposes*, Order No. 144, FERC Stats. & Regs. ¶ 30,254 at 31,531 (1981), *reh'g denied*, Order No. 144-A, FERC Stats. & Regs. ¶ 30,340 (1982), *aff'd*, *Public Systems v. FERC*, 709 F.2d 73 (D.C. Cir. 1983); *Lakehead Pipe Line Co.*, 71 FERC ¶ 61,338 at 62,314 (1995).

allowance in that proceeding.¹⁸ The Commission initiated the policy inquiry in Docket No. PL05-5-000 in response to the court's directive. For that reason, given the circumstances of this proceeding and other factors,¹⁹ the Commission allowed NTD Path 15 to recover the tax allowance, subject not only to refund but also to the outcome of the proceeding in Docket No. PL05-5-000. We have now examined the issue in Docket No. PL05-5-000, and, based upon our findings in that proceeding, we will permit NTD Path 15 to retain the income tax allowance if it can demonstrate (in a filing ordered below) that NTD Path 15 meets the standard set out in Docket No. PL05-5-000. Accordingly, we deny rehearing on this issue.

14. TANC further contends that, because NTD Path 15 made its Revenue Requirement and TO Tariff Filing after it knew that the Commission's income tax allowance policy was in question, the Commission should not have grandfathered NTD Path 15 under the pre-*BP West* policies, but should have applied the new policy determined in Docket No. PL05-5-000.

15. We disagree with TANC's characterization of the December 2 Order as grandfathering NTD Path 15 under the pre-*BP West* policies. In the December 2 Order, the Commission accepted the income tax allowance, but specifically made it subject to refund and subject to the outcome of the inquiry in Docket No. PL05-5-000. No grandfathering occurred. Rather, the Commission ensured that it would be able to adjust the rates and order refunds as necessary based on the outcome of Docket No. PL05-5-000. Accordingly, we deny this request for rehearing.

16. TANC adds that the Commission erred by failing to rule that, after the proceeding in Docket No. PL05-5-000, it would take additional action in this proceeding in the form of a final order that could be appealed. We disagree. As previously explained, the Commission accepted the tax allowance subject to refund and subject to the outcome of the inquiry in Docket No. PL05-5-000. This essentially ensured that the Commission would have to issue another order in Docket No. ER05-17-000. Indeed, pursuant to the policy statement that the Commission is issuing concurrently in Docket No. PL05-5-000, NTD Path 15 will be permitted an income tax-allowance on the income imputed to the corporation or to the partners or the members of pass-through entities, provided that the corporation or the partners or the members have an actual or potential income tax liability

¹⁸ *BP West*, 374 F.3d 1263 at 1312.

¹⁹ *See supra* P 10.

on that public utility income.²⁰ To make such a showing, an entity would have to make a filing with the Commission. Therefore, under the circumstances of this proceeding, we will direct NTD Path 15 to make a compliance filing within 30 days of the date of this order demonstrating that it meets the standard set out in Docket No. PL05-5-000.²¹ Consequently, TANC's argument on the need for further action in Docket No. ER05-17-000 is moot.

17. NTD Path 15 states that, since the Commission accepted its proposed Base Case Revenue Requirement, there was no need for further consideration of the proposed Alternative Case Revenue Requirement that would have incorporated a pre-tax return on common equity of approximately 22.78 percent. Nonetheless, NTD Path 15 requests that the Commission clarify that it did not intend to prejudge NTD Path 15's right to a pre-tax equity return because the Commission might determine in Docket No. PL05-5-000 that a pre-tax equity return is an appropriate policy response to *BP West*. NTD Path 15 contends that, permitting an adjusted equity return in lieu of a tax allowance, would simply preserve the attributes of the CPUC Settlement's negotiated rate terms. It adds that, assuming that the CPUC Settlement does limit NTD Path 15's equity return to 13.5 percent on a pre-tax basis, the Commission's consideration and adoption of a new policy to address the rate-making implications of *BP West* constitutes a significant

²⁰ In the policy statement on income tax allowance that the Commission is issuing concurrently in Docket No. PL05-5-000, the Commission "concludes that it should return to its pre-*Lakehead* policy and permit an income tax allowance for all entities or individuals owning public utility assets, provided that an entity or individual has an actual or potential income tax liability to be paid on that income from those assets. Thus a tax-paying corporation, a partnership, a limited liability corporation, or other pass-through entity would be permitted an income tax allowance on the income imputed to the corporation, or to the partners or the members of pass-through entities, provided that the corporation or the partners or the members, have an actual or potential income tax liability on that public utility income. Given this important qualification, any pass-through entity seeking an income tax allowance in a specific rate proceeding must establish that its partners or members have an actual or potential income tax obligation on the entity's public utility income. To the extent that any of the partners or members do not have such an actual or potential income tax obligation, the amount of any income tax allowance will be reduced accordingly to reflect the weighted income tax liability of the entity's partners or members." *Policy Statement on Income Tax Allowances*, 111 FERC ¶ 61,139 at P 32 (2005).

²¹ *Id.*

circumstantial change that the parties to the settlement could not have reasonably contemplated when they memorialized the rate terms of the CPUC Settlement and thus the CPUC Settlement may be challenged and reviewed.²² In the policy statement that the Commission is issuing concurrently in Docket No. PL05-5-000, the Commission does not adopt the adjusted, pre-tax return on common equity proposal espoused by NTD Path 15; therefore, this issue is now moot. Accordingly, we deny NTD Path 15's request for rehearing.

The Commission orders:

(A) The requests for rehearing filed by TANC and NTD Path 15 are hereby denied, as discussed in the body of this order.

(B) NTD Path 15 is hereby directed to submit a compliance filing within 30 days of the date of this order, as discussed in the body of this order.

By the Commission.

(S E A L)

Linda Mitry,
Deputy Secretary.

²² *Citing Tesoro Alaska Petroleum Co. v. FERC*, 234 F.3d 1286, 1290-91 (D.C. Cir. 2000).