UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Midwest Independent Transmission System Operator, Inc., and FirstEnergy Services Company — Docket No. ER06-532-000

ORDER CONDITIONALLY ACCEPTING AND SUSPENDING TARIFF REVISIONS

(Issued March 16, 2006)

1. In this order we address proposed changes to American Transmission Systems, Inc.'s (American Transmission) transmission rate formula in Attachment O to the Midwest Independent Transmission System Operator, Inc.'s (Midwest ISO) Open Access Transmission and Energy Markets Tariff (TEMT). We conditionally accept the proposed changes, suspend them for a nominal period and make them effective April 1, 2006, subject to refund and subject to the outcome of ongoing proceedings in Docket No. ER05-6, *et al*.

I. **Background**

2. On January 24, 2006, Midwest ISO and First-Energy Services Company (First Energy), on behalf of American Transmission, (collectively, Applicants) filed proposed revisions to American Transmission's transmission rate formula in Attachment O to the TEMT. Applicants request that the proposed revisions be accepted to become effective April 1, 2006.

3. American Transmission, a stand-alone transmission company and a subsidiary of First-Energy, is a transmission-owning member of Midwest ISO, and transmission service over the American Transmission system is provided under the Midwest ISO TEMT. Attachment O to the TEMT contains formulas used in calculating rates for transmission service under the TEMT, including the license plate zonal rates for transmission service for delivery within each transmission owner's zone. The Attachment O formula uses Form No. 1 investment cost, operating cost, and revenue data from the prior calendar year to calculate a transmission owner's revenue requirement and rates for the rate year beginning each June 1. Under the Attachment O formula, a transmission owner's license plate zonal rates are calculated by first reducing its gross transmission revenue requirement, *i.e.*, its total transmission cost-of-service, by revenue credits to account for revenues received from sources other than the load in the

transmission owner's zone, such as the transmission owner's share of revenue from through and out service. Once the revenue credits are subtracted from the gross transmission revenue requirement (yielding the net zonal revenue requirement), the net zonal revenue requirement is divided by the sum of network load and long-term point-to-point reservations for delivery within the zone, to derive the transmission owner's license plate zonal rates. Reducing the gross revenue requirement by the amount of these outside revenues ensures that the transmission owner does not over-recover its revenue requirement.[1]

4. Through Schedules 18 and 19 of the TEMT, American Transmission has continued to recover, from sources other than load in its license plate pricing zone, revenues that would have been lost due to the elimination of rate pancaking for transmission service within Midwest ISO, for a transition period commencing October 1, 2003, when it became a transmission-owning member of Midwest ISO, through October 31, 2005.[2] In addition, pursuant to a series of Commission orders, on December 1, 2004, a new pricing structure took effect that eliminated rate-pancaking for transmission service between Midwest ISO and PJM Interconnection, LLC (PJM) and replaced it with a license plate rate design for service over the combined Midwest ISO/PJM region, together with a transitional rate mechanism to recover revenues that would have been lost due to the elimination of rate pancaking during a 16-month transition period ending March 31, 2006.[3] This transitional lost revenue recovery adopted in the November 18, 2004 Order is provided in Schedule 21 of the TEMT.

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[1] Without including the revenue credits for, as relevant here, through and out service revenue from sources other than the load in its zone, a transmission owner would recover its full revenue requirement through its zonal rates. If the transmission owner then received additional revenue from outside sources, for example, in the form of through and out rate revenue, the transmission owner would over-recover its revenue requirement.

[2] *Midwest Independent Transmission System Operator, Inc*., 103 FERC ¶ 61,090 (2003), *order approving settlement*, 106 FERC ¶ 61,200 (2004).

[3] The replacement rate mechanism, called the Seams Elimination Charge/Cost Adjustment/Assignment (or SECA), is currently subject to an ongoing proceeding in Docket No. ER05-6, *et al. See Midwest Independent Transmission System Operator, Inc.*, 109 FERC ¶ 61,168 (2004) (November 18, 2004 Order), *order on clarification*, 109 FERC ¶ 61,243 (2005).

II. **Description of Filing**

5. Applicants state that the proposed changes to American Transmission's formula rate are necessary to account for the permanent elimination of revenues from sources other than the load in its zone resulting from the elimination of through and out rates (that resulted in rate pancacking in the Midwest ISO/PJM region). Applicants assert that, although the elimination of through and out rates became effective December 1, 2004, revenues associated with such service from sources other than load in American Transmission's zone have continued through the transitional SECA adopted by the Commission and the continuation of through and out rates for certain pre-existing transactions, both of which will expire on March 31, 2006.[4] Because the formula rate is based on past calendar-year data, once the SECA expires, these revenues associated with through and out service would continue to be reflected as a revenue credit after March 31, 2006,[5] even though American Transmission will no longer be receiving these revenues.

6. Therefore, Applicants propose the Revenue Credit Correction, to account for the permanent elimination of these revenues. The Revenue Credit Correction adds a line to American Transmission's Attachment O formula, under the Revenue Credit section, to reduce the total revenue credits by the amount of the eliminated stream of revenues from sources other than the load in the transmission owner's zone.[6] This will reduce American Transmission's revenue credits and increase its net zonal revenue requirement, resulting in recovery of more of its revenue requirement through its license plate zonal rates.

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[4] In addition to the transitional SECA, the Commission also allowed the continuation of through and out rates for certain existing reservations for through and out service – those pursuant to requests made before November 17, 2003, and those reservations commencing before April 1, 2004. *See Midwest Independent Transmission System Operator, Inc.*, 104 FERC ¶ 61,105, *order on reh'g*, 105 FERC ¶ 61,212 (2003).

[5] Applicants explain that, under the Attachment O transmission rate formula, American Transmission's gross revenue requirement is reduced by revenue credits to account for revenue received from the continuation of through and out rates for existing transactions (e.g., Schedules 7, 8 and 14 of the TEMT) and from the transitional rate mechanisms (*i.e*., Schedules 18, 19 and 21).

[6] Applicants' proposed tariff revisions add Line 36a, titled "transmission charges associated with revenue credit correction," to page 4 of American Transmission's Attachment O formula rate. Added Note V explains that the amounts to be entered on Line 36a, are from Account 456, other electric revenues, of American Transmission's Form No. 1. Note V also provides that the formula will be updated to reflect any modifications, ordered by the Commission, to the revenues associated with the Revenue Credit Correction in Line 36a.

Applicants state that the annual increases to American Transmission's zonal revenue requirement as a result of the Revenue Credit Correction would be $2.35 million for the rate year ending May 31, 2006, based on actual calendar-year 2004 data, $39.2 million for the rate year ending May 31, 2007, based on estimated calendar-year 2005 data, and $6.0 million for the rate year ending May 31, 2007, based on estimated calendar-year 2006 data.

7. Applicants argue that the Revenue Credit Correction is consistent with basic cost recovery and ratemaking principles. Applicants argue that their proposal would maintain American Transmission's existing cost of service and gross revenue requirement, and add that, absent the proposed Revenue Credit Correction, American Transmission would be unable to recover its full revenue requirement until June 1, 2008, due to the lag in the reflection of Form No. 1 data in the rates. Applicants explain that American Transmission's Attachment O formula rate assumes that costs and revenues for the prior calendar year are generally representative of the current rate year's costs and revenues. However, on April 1, 2006, once revenues associated with through and out service are permanently eliminated, Applicants explain, the rates produced under the current Attachment O formula rate will no longer adequately represent American Transmission's actual revenues because the revenue credits will include amounts for revenues that American Transmission no longer receives. Although the transmission rate formula would eventually update to reflect the eliminated revenues, this would not occur until June 1, 2008, and, according to Applicants, American Transmission would significantly under-recover its revenue requirement from April 1, 2006 through May 31, 2008.

8. Because this problem arises as a result of the Commission's elimination of through and out rates, and the Revenue Credit Correction is necessary to allow American Transmission to fully recover its revenue requirement upon the termination of the transitional SECA lost revenue recovery mechanism on March 31, 2006, Applicants assert that the proposed changes should be accepted to become effective April 1, 2006.

III. Notice and Responsive Pleadings

9. Notice of Applicants' filing was published in the *Federal Register*, 71 Fed Reg. 5,827 (2006), with interventions and protests due on or before February 14, 2006. Midwest Stand-Alone Transmission Companies filed a timely motion to intervene, American Municipal Power-Ohio, Inc. (AMP-Ohio) filed a motion to intervene and protest, and the Public Utilities Commission of Ohio (Ohio Commission) filed a motion to intervene out-of-time.

10. AMP-Ohio asserts that American Transmission's proposal would result in American Transmission recovering more of its costs from load within its license plate pricing zone, which includes AMP-Ohio's load. AMP-Ohio argues that the instant proposal is unjust and unreasonable because it proposes to update the formula rate to

reflect changes in current conditions to the benefit of American Transmission, yet ignores other changes that would lower American Transmission's transmission rates. AMP-Ohio asserts that a formula rate presents both benefits and burdens and, although American Transmission's actual revenues may be less, this is an inherent risk in adopting a formula rate.

11. AMP-Ohio asserts that, when American Transmission first proposed to use the Midwest ISO Attachment O formula rate, the Commission had already issued orders to eliminate through and out rates between Midwest ISO and PJM. That is, American Transmission was aware of the upcoming cessation of revenues from sources other than its zonal load for through and out service, yet did not seek to modify the formula rate when it proposed to adopt that formula rate in its December 2, 2004 filing in Docket No. ER05-285-000.

12. AMP-Ohio argues that, should the Commission allow the Revenue Credit Correction, it should require American Transmission to update other inputs to the formula rate that may offset the zonal rate increases under the Revenue Credit Correction. AMP-Ohio states that the return on equity is one element of the formula rate that should be adjusted to account for known changes. AMP-Ohio argues that the return on equity under the Attachment O formula was derived based on the midpoint of the returns of a proxy group that included, at the top of the range, the return of a company that no longer participates in the Midwest ISO. AMP-Ohio argues that the return on equity should be adjusted to remove that company, which would result in a 53 basis point reduction in the return on equity. AMP-Ohio also argues that, if forecasted net plant is lower, or if forecast load is greater, than the prior calendar year, these changes should effectively reduce American Transmission's zonal rates.

13. Finally, AMP-Ohio asserts that the Commission should also require an adjustment in the event that, through the regionalization of cost recovery of certain facilities or other circumstances, American Transmission receives additional revenues from sources other than load within its transmission zone.

IV. Discussion

14. Pursuant to Rule 214 of the Commission's rules of Practice and Procedure, 18 C.F.R. § 385.214 (2005), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. We will grant Ohio Commission's untimely intervention, given its interest, the early state of this proceeding, and the absence of undue prejudice or delay.

15. Applicants' proposed tariff changes to incorporate the Revenue Credit Correction will be accepted for filing, and suspended for a nominal period, to become effective April 1, 2006, subject to refund and to the outcome of Docket No. ER05-6, *et al.*, as

described below. Under the proposed changes to the formula rate, revenue credits would continue to be calculated using the same historic test period that is used to calculate other inputs to the formula rate, but the manner in which that test period data is reflected is changed to reflect the change in the rate design for through and out service in the Midwest ISO/PJM region. The requested changes to the Attachment O formula rate are necessary to provide American Transmission the opportunity for full recovery of its revenue requirement, given the change in rate design for through and out service in the Midwest ISO/PJM region.

16. AMP-Ohio argues that American Transmission should not be allowed to make adjustments to one input of the formula rate (*e.g.*, revenue credits) without examining other inputs that may have the effect, if updated, of lowering the transmission rate. AMP-Ohio would have American Transmission update other aspects of the formula rate, such as the return on equity, in an effort to offset the increase to zonal rates under the proposed Revenue Credit Correction. We disagree with AMP-Ohio. The Commission has previously found it unnecessary to require updated cost-of-service analysis to evaluate adjustments to license plate zonal rates to reflect the change in rate design associated with the elimination of rate pancaking.[7] Additionally, the proposed changes to the formula rate will be made subject to the outcome of the proceeding in Docket No. ER05-6, *et al.*

17. Finally, it appears that Applicants' proposed tariff sheets are in error. According to Applicants' transmittal letter, the newly added Line 36a is intended to reduce American Transmission's revenue credits by an amount corresponding to the eliminated stream of revenues for through and out service. However, Line 37 of page 4 of Attachment O, the total for "Other Electric Revenues," does not reflect the subtraction of the Revenue Credit Correction amount in new Line 36a. Therefore, we direct Applicants to correct this omission in a compliance filing, within 30 days of the date of this order.[8]

The Commission orders:

(A) Applicants' proposed tariff revisions are hereby conditionally accepted for filing, and suspended for a nominal period to become effective April 1, 2006, as requested, subject to refund and to the outcome of the proceeding in Docket No. ER05-6, *et al.*, as discussed in the body of this order.

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[7] *See Midwest Independent Transmission System Operator, Inc.*, 105 FERC ¶ 61,212 at P 49 (2003).

[8] It appears that Line 37 should read "Total of (a)-(b)-(c)…" as is the case in the formula rate workpapers in Applicants' Exhibit FE-2.

(B) Within 30 days of the date of this order, Applicants are hereby directed to make a compliance filing to correct the proposed tariff sheets, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.