

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

NorthWestern Corporation

Docket No. EL06-105-000

ORDER GRANTING DECLARATORY ORDER

(Issued December 22, 2006)

1. On September 12, 2006, NorthWestern Corporation (NorthWestern) submitted a petition for declaratory order (Petition) seeking Commission approval to use a transmission rate design that allocates cost responsibility for new and expanded transmission facilities along two related but distinct transmission paths, according to the cost of the new facilities required to satisfy particular transmission service requests.¹ In this order, we grant NorthWestern's Petition and find that NorthWestern's proposal is consistent with the Commission's "Or" pricing policy.

I. Background

2. NorthWestern owns and operates transmission facilities located in Montana and South Dakota. NorthWestern maintains separate open access transmission tariffs (OATTs) for its operations in Montana and South Dakota because NorthWestern's Montana and South Dakota transmission facilities are neither physically interconnected, nor located in the same North American Electric Reliability Council region.

¹ NorthWestern refers to its proposal as "Enhanced Or" pricing. As described herein, its proposal is consistent with the Commission's "Or" pricing policy.

3. In 1999, Montana Power sold most of its electric generation facilities to PPL Montana,² and in 2001, Montana Power sold its transmission facilities to NorthWestern.³ NorthWestern also states that, because restructuring initiatives in Montana do not permit customers with load less than 50 kW to choose their supplier, it is the permanent default supplier for nearly all the electric customers in the area.

II. NorthWestern's Request for Declaratory Order

4. In its Petition, NorthWestern proposes to develop two separate incremental transmission rates for two transmission upgrade projects (Montana-to-Idaho Expansion and Eastern System Upgrades) and to allocate cost responsibility for the new transmission facilities based on the particular customer's transmission service request. NorthWestern seeks assurance that its pricing proposal is consistent with the Commission's transmission pricing policy so that it can further develop transmission rates for the projects.

5. NorthWestern states that it has received transmission service requests which exceed the capability of the existing transmission system. According to NorthWestern, the new transmission requests fall into two main groups, the Montana-to-Idaho Expansion and the Eastern System Upgrades.

6. The Montana-to-Idaho Expansion includes requests that were submitted in response to a 31-day open season, conducted in December 2004. In response to the open season, eight participants submitted transmission service requests totaling 2,250 MW. Ultimately, six participants submitted a required one-month reservation fee deposit for

² *Montana Power Co.*, 87 FERC ¶ 61,344 (1999).

³ *Montana Power Co. and NorthWestern Corp.*, 94 FERC ¶ 62,141 (2001). The Commission recently approved the acquisition of NorthWestern and its subsidiaries by Babcock & Brown Infrastructure Limited, an Australian-based utility infrastructure company that owns and manages infrastructure businesses worldwide. *NorthWestern Corp.*, 117 F.E.R.C. ¶ 61,100 (2006).

850 MW of upgrades/expansions to Western Electricity Coordinating Council (WECC) Path 18 extending from southwestern Montana to southern Idaho.⁴ NorthWestern states the new transmission facilities are expected to be in service in 2010.

7. The Eastern System Upgrades, according to NorthWestern, are needed to accommodate point-to-point transmission service requests to move approximately 184 MW of power from the eastern portion of NorthWestern's control area to an interconnection with Bonneville Power Administration (Bonneville) in the west, as well as 550 MW of transmission service requests for service to the Montana-to-Idaho Expansion.⁵ NorthWestern states that providing transmission capacity for these requests will require the proposed upgrades to the existing transmission system and may require the construction of additional new transmission lines in the eastern portion of NorthWestern's Montana control area.

8. NorthWestern expects to complete system impact studies by fall 2006, after which it will identify the transmission facilities needed, the costs to build or expand existing facilities and resulting rates. NorthWestern states that, in order to distribute illustrative rates once the system impact studies are completed, it seeks Commission authorization to develop separate incremental transmission rates for the two projects.⁶

9. NorthWestern describes its understanding of the Commission's current transmission pricing policy, which "permits the pricing of transmission service to reflect either the greater of the network's average cost (with expansion cost rolled-in) or the incremental cost of the expansion (known as 'Or' pricing), but prohibits pricing based on

⁴ Path 18 includes two fully-subscribed transmission lines: a 230 kV line (which extends from Montana to southern Idaho); and a 161 kV line (which also extends from Montana to southern Idaho). The current combined transmission capacity of Path 18 is 337 MW.

⁵ The Petition notes that certain point-to-point transmission service requests with an eastern point of receipt and the open season requests with an eastern point of receipt would both make use of the Eastern System Upgrades; therefore, NorthWestern explains, both sets of requests would be allocated Eastern System Upgrade costs, based on the capacity requested.

⁶ In support of its proposal, NorthWestern calculates illustrative transmission rates to demonstrate that rolled-in expansion costs would increase the transmission rates to NorthWestern's existing transmission customers. *See* Petition Exhibit A at 7.

a combination of average and incremental costs (known as ‘And’ pricing).”⁷ Moreover, existing users should be held harmless from costs related to new transmission service requests. NorthWestern states that its pricing proposal is structured so that the costs of the two projects (the Montana-to-Idaho Expansion and the Eastern System Upgrades) will not be combined or co-mingled to the disadvantage of those transmission customers who would not use the projects.⁸ In doing so, NorthWestern claims that its pricing proposal adheres to the “fundamental” theory of ratemaking, “that the costs should be recovered in the rates of those customers who utilize the facilities and thus cause the costs to be incurred,”⁹ and is both consistent with the Commission’s “Or” pricing policy and also satisfies the five principles set forth in the Commission’s Transmission Pricing Policy Statement.¹⁰

III. Notice, Interventions, Protests, and Comments

10. Notice of the NorthWestern’s filing was published in the *Federal Register*, 71 Fed. Reg. 56,513 (2006), with interventions and protests due on or before October 20, 2006. A motion to intervene and request for extension of time to file comments was filed

⁷ Petition at 12 n.17 (*citing Consumers Energy Co.*, 95 FERC ¶ 61,233 at 61,804 (2001) (citations omitted)).

⁸ NorthWestern interprets the Commission’s “Or” transmission pricing policy as requiring it to consolidate the costs of the two projects into a single aggregated cost that would be allocated to all new transmission service requests irrespective of the facilities used.

⁹ Petition at 13 (*citing Pacific Gas & Electric Co.*, 97 FERC ¶ 63,014 at 65,062 (2001) (citations omitted)). As noted below, in this regard NorthWestern is correct, a single rate is not required.

¹⁰ Petition at 14-15. According to NorthWestern, the Commission in its Transmission Pricing Policy Statement concluded that transmission pricing should: (1) satisfy the traditional revenue requirement; (2) reflect comparability; (3) promote economic efficiency; (4) promote fairness; and (5) be practical. *See Inquiry Concerning the Commission’s Pricing Policy for Transmission Service Provided by Public Utilities Under the Federal Power Act, Policy Statement*, 59 Fed. Reg. 55,031 (Nov. 3, 1994), FERC Stats. & Regs. ¶ 31,005, at 31,141-44 (1994), *order on reconsideration*, 71 FERC P 61,195 (1995).

on October 10, 2006, by PPL EnergyPlus, LLC and PPL Montana, LLC (collectively PPL).¹¹ The request for an extension of time was granted to and including November 6, 2006.

11. Bonneville filed a timely motion to intervene. Great Northern Power Development L.P. (Great Northern) and the Montana Consumer Counsel filed timely motions to intervene with comments. On November 6, 2006, PPL filed a motion to intervene, protest and request for hearing. NorthWestern filed an answer and on December 6, 2006, PPL filed a response to NorthWestern's answer.

12. PPL requests that the Commission reject NorthWestern's Petition or alternatively set the matter for hearing to further investigate the filing. PPL argues that the filing is defective, premature and unjust and unreasonable insofar as it would place the full burden of the cost of the proposed transmission expansions on new transmission customers. PPL argues that all transmission customers who will benefit from the proposed transmission expansions should bear a share of the costs for those facilities.

13. PPL argues that NorthWestern's proposal includes unfounded assumptions, lacks explanation regarding how certain aspects will be implemented and contains a number of questions regarding the queue priorities of different transmission customers and the benefit that those customers will draw from or costs that they will impose on NorthWestern's transmission system.

14. PPL also argues that NorthWestern's proposal: (1) ignores Commission precedent that requires that the "Or" pricing policy be applied only where it is shown that the proposed facilities would not be constructed "but for" the new service requested and that an inquiry must be made as to whether other transmission customers (including unbundled native load) would benefit from the new facilities; (2) fails to demonstrate that native load customers receive no significant benefits from the expansion; and (3) fails to consider whether NorthWestern's transmission system may need enhancements to ensure continued reliable transmission service to its existing native load customers, even in the absence of additional transmission service requests.¹²

¹¹ In its motion, PPL requested production of documents that NorthWestern identified as containing critical energy infrastructure information under 18 C.F.R. § 388.113 (2006). The parties reached an agreement for the exchange of the requested materials independent of any Commission determination.

¹² PPL Protest at 14-15 (*citing* NorthWestern 2005 Open Season Report).

15. Great Northern supports NorthWestern's proposal because, according to Great Northern, it properly matches cost incurrence with cost causation and is consistent with the Commission's standard, the higher of rolled-in or incremental pricing, rate design. However, Great Northern requests clarification of the example provide by NorthWestern where the incremental rate for the Montana-to-Idaho Expansion (\$12.06/kw-mo) and for the Eastern System Upgrades (\$3.37/kw-mo) both exceed NorthWestern's current rolled-in, embedded cost rate (\$3.01/kw-mo). Great Northern points out that the rate assigned to new transmission service using both sets of upgrades is shown as the sum of the cost of the upgrades (\$15.43/kw-mo). Great Northern seeks clarification that NorthWestern's methodology does not include a "higher of" embedded cost rate component in the event NorthWestern's embedded cost rate, if one of the projects is rolled-in, exceeds the incremental rate of that set of upgrades.

16. The Montana Consumer Counsel argues that NorthWestern's proposal lacks sufficient detail to allow the Commission to determine whether its conceptual rate design proposal satisfies the just and reasonable standard of section 205 of the Federal Power Act (FPA).¹³ The Montana Consumer Counsel also seeks clarification that, if the rolled-in transmission rates, including the new upgrades result in a rate that is lower than the current rolled-in rates NorthWestern should be required to charge the lower rolled-in rates. The Montana Consumer Counsel also requests that the Commission clarify that parties may challenge any specific rate proposals that NorthWestern may file.

17. NorthWestern responds that PPL's protest reflects a misunderstanding of its request and Commission policy, and is an attempt to delay transmission expansion in Montana. NorthWestern also argues that an evidentiary hearing is not necessary because it Petition raises no issues of material fact.

18. NorthWestern disagrees with PPL's assertion that before considering its pricing proposal the Commission must first be satisfied that the identified facilities will not provide significant benefits to the existing users of the transmission system such that they should be rolled into NorthWestern's existing transmission rates and charged to all transmission customers and NorthWestern as the default retail supplier. NorthWestern argues that Commission policy does not require a "but for" test and a separate benefits test. NorthWestern asserts that there is no separate benefits test, unless the proposed expansion does not pass the initial "but for" test.¹⁴ NorthWestern also explains that,

¹³ 16 U.S.C. § 824d (2000).

¹⁴ NorthWestern Answer at 10 n.17 (*citing* Exhibit A, Supplemental Affidavit of Dr. Henderson at 4-5).

while it has an obligation to address the “but for” issue, it is premature to answer that question before the Petition is granted. NorthWestern also states that this and other issues raised by PPL should be raised by PPL when a rate filing is made. NorthWestern argues that it is not, in this Petition, asking the Commission to prejudge any cost responsibility; rather, it seeks assurance that costs for transmission facilities constructed under the open season will not be combined to form one incremental transmission rate, but rather should be the subject of separate incremental transmission rates.

19. NorthWestern also clarifies that the pre-existing point-to-point requests have senior queue positions, and will be responsible for the costs of the transmission facilities necessary to serve their requests. NorthWestern explains that an open season participant will be responsible for the costs of constructing the transmission facilities necessary to serve its request (but not those costs incurred to serve other open season requests).

20. With respect to the issues raised by Great Northern, NorthWestern explains that Dr. Henderson’s Supplemental Affidavit provides a hypothetical example demonstrating that under NorthWestern’s proposal, users of both sets of upgrades would not pay a rate that includes any embedded costs.¹⁵

IV. Discussion

A. Procedural Matters

21. Pursuant to Rule 214 of the Commission’s Rules of Practice and Procedure, 18 C.F.R. § 385.14 (2006), the timely, unopposed motions to intervene serve to make those parties who filed them parties to this proceeding.

22. Rule 213(a)(2) of the Commission’s Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2006), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept NorthWestern’s and PPL’s answers because they have provided information that assisted our decision-making process.

B. Commission Determination

23. NorthWestern indicates that its transmission system cannot accommodate all the outstanding transmission requests for transmission service on its system. The

¹⁵ NorthWestern Answer at 13-14 (*citing* Exhibit A, Supplemental Affidavit of Dr. Henderson at 6-8).

construction of the Montana-to-Idaho Expansion and the Eastern System Upgrades are intended to alleviate the constraints.

24. We approve in principle NorthWestern's proposal, to develop separate incremental transmission rates for the respective projects. NorthWestern does not propose to charge an embedded cost rate for either project.

25. We find that NorthWestern's proposed transmission pricing structure is consistent with the Commission's current "Or" pricing policy as articulated in *Pennsylvania Electric Company (Penelec)*.¹⁶ In *Penelec*, the Commission stated that, if a transmission system is constrained and the transmission provider chooses to expand the system to remove the constraint, the utility may charge a transmission rate that does not exceed the higher of an embedded cost price or a price reflecting the incremental cost of expanding the system. This is referred to as "Or" pricing. Under NorthWestern's proposal, it will charge separate incremental transmission rates, based on the cost of those expanded or upgraded transmission projects necessary to provide the transmission service.

26. PPL asserts that, in order to charge incremental transmission rates, NorthWestern must demonstrate that the proposed facilities would not be constructed "but for" the new service and that an inquiry must be made as to whether other transmission customers (including unbundled native load) would benefit from the new facilities. These arguments are premature; they go to the specifics of the calculation of the incremental cost rates and not to the question before us, whether NorthWestern can charge separate incremental rates for its two separate projects. PPL may raise arguments regarding the basis and justification of NorthWestern's particular incremental rates when NorthWestern submits a FPA section 205 filing.

27. The Montana Consumer Counsel and Great Northern seek clarification that if the rolled-in transmission rates, including the new upgrades, are ultimately shown to be lower than current rolled-in rates, NorthWestern will be required to charge the lower rolled-in rates. In *Penelec*, however, the Commission concluded to the contrary that in this situation a utility is not required to charge lower rolled-in rates, but can charge higher incremental rates. That is, for transmission expansions "a utility may charge a rate that

¹⁶ 60 FERC ¶ 61,034, at 61,121-22 (1992), *reh'g denied*, 60 FERC 61,244, *aff'd sub nom. Pennsylvania Electric Co. v. FERC*, 11 F.3d 207 (D.C. Cir. 1993); *accord Allegheny Power Service Corp.*, 85 FERC 61,276 at 62,125 (1998); *Commonwealth Electric Company*, 72 FERC ¶ 61,295 at 62,262 n.1 (1995).

does not exceed *the higher* of (a) its embedded costs, or (b) opportunity costs capped at the utility's incremental cost of expansion to relieve the constraint.”¹⁷ This ensures a just and reasonable cost-based transmission rate.¹⁸

28. At such time as NorthWestern makes a FPA section 205 filing, the Montana Consumer Counsel and Great Northern, like PPL, may raise issues regarding the rate calculation and all underlying assumptions. Therefore, notwithstanding our approval in principle of NorthWestern’s conceptual pricing proposal here, any proposed rates that are filed in compliance with NorthWestern’s FPA section 205 obligations will undergo Commission review to determine that they are just and reasonable and not unduly discriminatory or preferential.

29. In sum, we conclude that NorthWestern’s pricing proposal is consistent with the Commission’s “Or” transmission pricing policy and, as such, NorthWestern is permitted to develop separate incremental transmission rates reflecting the costs of the two projects (Montana-to-Idaho Expansion and Eastern System Upgrades), and to allocate the costs to customers based on their particular transmission service requests.

The Commission orders:

NorthWestern’s Petition for declaratory order is hereby granted, as discussed in the body of this order.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.

¹⁷ *Penelec*, 60 FERC at 61,124 (citation omitted) (emphasis added).

¹⁸ *Id.* at 61,123.