



Federal Energy Regulatory Commission
December 21, 2006
Open Commission Meeting
Talking Points of
Commissioner Suedeen Kelly

Item E-1: Promoting Transmission Investment through Pricing Reform (RM06-4-001)

- FPA section 219 calls for the Commission to issue a rule designed to “benefit consumers by ensuring reliability and reducing the cost of delivered power by reducing transmission congestion” and which promotes “reliable and economically efficient transmission and generation of electricity.”
- I am pleased to join my colleagues in supporting this order because it now makes clear that section 219’s important goals are paramount. In short, it makes several significant clarifications to the Final Rule that go to the very heart of section 219—that is, that ultimately it is the consumer that must benefit from the rule.
- A number of commenters on the Final Rule raised concerns that the Final Rule did not reflect the fact that the incentives’ direct costs will ultimately be borne by consumers. This order addresses this concern in two significant ways. First, it sets forth a rigorous nexus test, and second, it clarifies that ROE incentives will not be handed out lightly.
- It makes clear that applicants will not receive incentives simply by asking for them, or by merely stating that incentives are needed to attract capital. Nor will applicants be rewarded just for the sake of building new transmission.
- Rather, as today’s order makes clear, applicants must show a meaningful causal connection between the requested incentives and the demonstrated risks and challenges it faces in building proposed transmission facilities. I believe this nexus test is consistent with the underlying principles of incentive rate treatment—that is, it will incite applicants to action, rather than simply reward them for the mere sake of building transmission facilities.
- I’m also pleased about the clarifications regarding the process for approving requests for incentive ROEs. First, today’s order points out that, where an applicant seeks multiple incentives under the Final Rule, such as CWIP in rate base and recovery of abandoned plant, the Commission will consider the effect these incentives may have on risk, and whether these incentives will lower overall risk such that a request for an ROE in the upper end of the zone of reasonableness may not be appropriate.
- Equally important, this order states that we will not routinely grant ROE incentives routinely, and when we do grant them, we have no expectation of routinely granting them at the top end of the zone of reasonableness. Instead, applicants must justify a higher ROE, and then justify where in the zone of reasonableness that return should lie.
- I believe these significant clarifications are consistent with meeting the specific consumer-benefiting purposes of Section 219. They are also consistent with court precedent, which holds that, when the Commission

considers non-cost factors in setting rates, we must always relate our action “to the primary aim of the Act to guard the consumer against excessive rates.”

- Of course, the devil is always in the detail. Because we will look at each request for incentive rate treatment under section 219 on a case-by-case basis, there are many important issues that the Final Rule cannot meaningfully address, but rather, that are more appropriately considered at the implementation stage. For example, when an applicant seeks a package of incentives, and we determine that the applicant has asked for too much—that is, that it may not result in a rate that is just, reasonable, and not unduly discriminatory--the rule is silent as to how we will pick and choose among the requested incentives.
- As one commenter noted, an applicant may place too many incentives on its wish list, or may select incentives options that are poorly tailored to its factual situation. I agree with commenters that, faced with any incentive request, the Commission should recognize that it may be inflated, and should “always ask whether every dollar the applicant will collect represents the most congestion-reducing or reliability-ensuring way to spend the next dollars of society’s investment in transmission facilities and technologies.” In other words, the Commission should choose the incentives that, in a particular case, will best advance the purposes of section 219, that is, that the consumer ultimately benefits.
- This is particularly important because the Final Rule does not require applicants to provide a cost-benefit analysis for incentive-based rate treatment. While I agree with this determination, I do so because I believe that firm implementation of our Final Rule, which includes an analysis that identifies which incentives are best-tailored to overcome the demonstrable risks and challenges facing the project, and at the least cost to the consumer, will result in a process that is an appropriate substitute for a cost-benefit analysis.
- I did want to add a note or two in response to concerns raised over our determination that we will allow single-issue ratemaking for new transmission projects. First, I want to emphasize that single-issue ratemaking is a significant incentive, and one that the Commission has allowed only under very limited circumstances in the past. Second, I want to reiterate that we will, on a case-by-case basis, balance the need for new infrastructure, and the importance of allowing single issue ratemaking in support of that infrastructure, with the concerns over whether a specific mechanism is required to re-open existing rates or whether the traditional complaint processes are sufficient for that purpose.
- Finally, as we acknowledged in issuing the Final Rule, we have identified specific incentives that will be allowed under certain circumstances, some of which reflect a departure from the kinds of incentives we have allowed in the past. The Final Rule also departs from prior Commission practice by providing greater flexibility with respect to the nature and timing of rate recovery for needed transmission facilities.

- Needless to say, these are significant changes to the way we have done business. However, in my view, today's order goes a long way towards ensuring that, with firm implementation, the Final Rule will benefit consumers by ensuring reliability and reducing the cost of delivered power by reducing transmission congestion.
- How will we know that the Final Rule is meeting these important goals? It is my hope that in adopting an annual reporting requirement (FERC Form 730) for utilities that receive incentive rate treatment for specific transmission projects, the Commission will have the necessary information regarding projected investments as well as information about completed projects to accurately monitor the success of the ratemaking reforms set forth in the Final Rule. I am interested in exploring with my colleagues avenues for ensuring that the annual reporting requirements sufficiently monitor the Final Rule, and perhaps even consider preparing periodic Commission reports that reflect the results of such monitoring.
- In closing, I want to express my sincere appreciation to staff for its Herculean efforts from start to finish on this rule. I know it wasn't easy or fun. But your hard work has resulted in a Final Rule that we can all be proud of. Thank you. And with that, I am pleased to vote this order out.