FEDERAL ENERGY REGULATORY COMMISSION

WASHINGTON, D.C. 20426

NEWS RELEASE

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FOR IMMEDIATE RELEASE
December 2, 2004
Docket Nos. PL05-5-000 and ER05-17-000

COMMISSION SETS INQUIRY ON INCOME TAX ALLOWANCES

The Federal Energy Regulatory Commission today launched an inquiry into its treatment of income tax allowances in cost-of-service ratemaking proceedings involving limited liability partnerships. The inquiry and provisions of a companion order issued today address a July 20, 2004 appeals court opinion finding inadequate the Commission's justification for its income tax allowance policy.

The Court of Appeals for the District of Columbia Circuit ruling, *BP West Coast Producers, LLC v. FERC,* was an outgrowth of an appeal in an oil pipeline rate case involving SFPP, L.P. The Commission's inquiry seeks comments "on whether the court's ruling applies only to the specific facts of the SFPP, L.P. proceeding, or also extends to other capital structures involving partnerships and other forms of ownerships."

Among other issues, the Notice of Inquiry asks commenters to address whether the court's reasoning applies to partnerships in which: (1) all the partnerships interests are owned by investors without intermediary levels of ownership; (2) the only intermediary ownership is a general partnership; (3) all the partnership interests are owned by a corporation; and (4) the corporate ownership of the partnership interests is minimal.

In a separate order also issued today, the Commission addressed a revenue requirement filing for a key transmission project in California, noting that the foundation for the financing and investment was based on the Commission's ruling on cost-of-service issues for the project prior to the July appeals court decision. The Commission ordered a hearing for Trans-Elect NTD Path 15 LLC's filing and encouraged the parties to pursue settlement.

Under the Commission's cost-of-service ratemaking principles, the return on common equity allocated to the corporate owners of a partnership is taxable and a public utility is permitted a corresponding income tax allowance in its revenue requirement. The Commission noted that a change in policy in the income tax allowance in the Trans-Elect case would involve approximately $7.7 million, or about 20.9 percent of the requested revenue requirement of the $306 million transmission project. The project is critical to relieving constraint in California's north-south power flows, allowing needed power to flow to California's growing markets.

BP West and its application may represent a generic issue that must be viewed in the context of all the industries FERC regulates, the Commission said. Since Trans-Elect went forward with its project based on a June 2002 ruling by the Commission, the Commission today said it would allow Trans-Elect to include an income tax allowance associated with its 13.5 percent return on common equity for the first three years in which the rates are fixed. The allowance is subject to refund, however, pending the outcome of the Notice of Inquiry proceeding.

Comments on the Notice of Inquiry (Docket No. PL05-5-000) must be filed with the Commission by December 22, 2004.

R-04-57 (30)