Nos. 09-2052 and 09-2053 (Consolidated)

In the United States Court of Appeals for the Fourth Circuit

OFFICE OF THE ATTORNEY GENERAL OF VIRGINIA, DIVISION OF CORPORATION COUNSEL, *et al*.
PETITIONERS,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
RESPONDENT.

ON PETITIONS FOR REVIEW OF ORDERS OF THE FEDERAL ENERGY REGULATORY COMMISSION

BRIEF FOR RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

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TABLE OF CONTENTS

TABLE OF CONTENTS

PAGE

TABLE OF AUTHORITIES

COURT CASES: **PAGE**

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES

ADMINISTRATIVE CASES: **PAGE**

STATUTES:

REGULATIONS:

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BRIEF OF RESPONDENT FEDERAL ENERGY REGULATORY COMMISSION

STATEMENT OF THE ISSUE

Whether the Federal Energy Regulatory Commission (FERC or Commission) reasonably approved the recovery of costs of Virginia Electric and Power Company, doing business as Dominion Virginia Power (Dominion), related to Dominion's joining and participating in a FERC-approved Regional Transmission Organization (RTO), where such costs were prudently-incurred

wholesale costs which under Commission policy were fully recoverable in Dominion's wholesale rates.

STATUTORY AND REGULATORY PROVISIONS

The pertinent statutes and regulations are contained in the Addendum to this brief.

COUNTER-STATEMENT OF JURISDICTION

Petitioners, the Office of the Attorney General of Virginia, Division of Consumer Counsel, and the Virginia State Corporation Commission (collectively the Virginia Parties) invoke this Court's jurisdiction under Federal Power Act (FPA) § 313, 16 U.S.C. § 825*l*(b). However, as discussed in Argument Section II (B)(2) below, the Court lacks jurisdiction to hear the Virginia Parties' arguments that the Commission improperly failed to distinguish between RTO start-up costs and RTO administrative costs for purposes of Dominion's rate recovery (Br. 26-27, 29-30), as the Virginia Parties did not make these arguments on rehearing before the Commission, as 16 U.S.C. § 825*l*(b) requires.

On rehearing (*see* Virginia Parties' Rehearing Requests at JA 197-241), the Virginia Parties argued that the Commission should disapprove recovery of *all* of Dominion's deferred RTO costs -- which included both RTO start-up costs and RTO administrative costs -- without distinguishing in any manner between the two categories. The Virginia Parties made no argument whatsoever to the

Commission, as they do now to this Court, that RTO administrative costs could or should be treated any differently than are RTO start-up costs.

Having failed to argue on rehearing that RTO start-up costs and RTO administrative costs could or should be treated differently, the Virginia Parties cannot now be heard to argue that FERC erred in failing to make such a distinction. As this Court has recognized, its review of FERC orders "is limited by 16 U.S.C. § 825*l*, which provides, 'No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure to do so.'" *Mt. Lookout-Mt. Nebo Property Protection Ass'n v. FERC*, 143 F.3d 165, 173 (4th Cir. 1998). Therefore, the Virginia Parties' claims based upon the distinction between RTO administrative and RTO start-up costs are jurisdictionally barred.

STATEMENT OF THE CASE

On September 12, 2008, Dominion filed under FPA § 205, 16 U.S.C. 824d, to recover certain categories of Regional Transmission Organization costs, including costs incurred in the (unsuccessful) development of the Alliance RTO, costs incurred to join the PJM Interconnection, L.L.C. (PJM) RTO, and PJM RTO administrative fees. Dominion had deferred collection of these costs pending

expiration of a retail rate freeze that precluded passing on to retail ratepayers their share of the RTO costs incurred.

In the challenged Orders, the Commission permitted Dominion's requested cost recovery, finding that the costs Dominion sought to recover were wholesale costs, subject to FERC jurisdiction, that were fundamentally related to Dominion's efforts to participate in an RTO. *Virginia Electric and Power Co*., 125 FERC ¶ 61,391 (2008) (Tariff Order), *on reh'g*, 128 FERC ¶ 61,026 (2009) (Rehearing Order). Under Commission policy, recognizing the role that RTOs play in the development of competitive electricity markets, the Commission permits transmission owners such as Dominion to recover through special surcharges their costs in seeking to join an RTO, as well as their ongoing administrative fees related to their participation in the RTO.

On rehearing, the Virginia Parties argued that the Commission's approval of the deferred cost recovery constituted retroactive ratemaking as it adjusted prospective rates to make up for an alleged shortfall in prior rates. The Virginia Parties also asserted that, prior to approving recovery of these deferred costs, the Commission was required: (1) to find that Dominion had not already received sufficient retail revenues during the retail rate freeze to cover the RTO costs; and (2) to find that Dominion was legally unable to pass through the RTO costs to retail ratepayers at the time they were incurred.

The Commission rejected these contentions. Recovery of the deferred costs did not constitute retroactive ratemaking because the costs were not incurred for past service; rather, the costs were being charged to customers at the time they were enjoying the benefits of RTO participation, and ample notice had been provided to ratepayers that these deferred costs may be subject to recovery in the future. The Virginia Parties proffered no evidence that Dominion had already recovered these costs in its retail rates, which were frozen under state law prior to the time that the RTO costs were incurred. In any event, the question of whether Dominion had already received sufficient revenues under its retail rates to cover these costs, or whether state law permitted Dominion to pass through these costs to retail ratepayers during the retail rate freeze, were state law questions of retail rate recovery beyond the Commission's statutory authority.

STATEMENT OF FACTS

I. ORDER NO. 2000

In its Order No. 2000,[1] the Commission encouraged the voluntary interconnection and coordination of transmission facilities into regional districts by utilities "for the purpose of assuring an abundant supply of electric energy through the United States with the greatest possible economy." Order No. 2000 at 31,039.

[1] *Regional Transmission Organizations*, Order No. 2000, FERC Stats. & Regs. ¶ 31,089 (1999), *on reh'g*, Order No. 2000-A, FERC Stats. & Regs. ¶ 31,092 (2000), *petitions for review dismissed*, *Public Util. Dist. No. 1 of Snohomish County, Washington v. FERC*, 272 F.3d 607 (D.C. Cir. 2001).

The Commission explained the benefits RTOs provide for consumers:

> Regional institutions can address the operational and reliability issues now confronting the industry, and eliminate any residual discrimination in transmission services that can occur when the operation of the transmission system remains in control of a vertically integrated utility. Appropriate regional transmission institutions could: (1) improve efficiencies in transmission grid management; (2) improve grid reliability; (3) remove remaining opportunities for discriminatory transmission practices; (4) improve market performance; and (5) facilitate lighter handed regulation. Thus we believe that appropriate RTOs could successfully address the existing impediments to efficient grid operation and competition and could consequently benefit consumers through lower electricity rates resulting from a wider choice of services and service providers. In addition, substantial cost savings are likely to result from the formation of RTOs.

Id. at 30, 993. As the Supreme Court recently explained, the Commission has undertaken various initiatives in recent years "to break down regulatory and economic barriers" and "to reduce technical inefficiencies caused when different utilities operate different portions of the grid independently," most notably by "encourage[ing] transmission providers to establish 'Regional Transmission Organizations' – entities to which transmission providers would transfer operational control of their facilities for the purpose of efficient coordination." *Morgan Stanley Capital Group v. Pub. Util. Dist. of Snohomish County*, 128 S. Ct. 2733, 2740-41 (2008).

To encourage RTO development and participation, Order No. 2000 directed transmission-owning utilities (like Dominion) either to participate in an RTO or to

explain their refusal to do so. *Midwest ISO Transmission Owners v. FERC*, 373 F.3d 1361, 1365 (D.C. Cir. 2004). Also to encourage participation, Order No. 2000 "assure[d] utilities that they will not be penalized for RTO participation," Order No. 2000 at 31,172, and clarified that "the reasonable costs of developing an RTO may be included in transmission rates." *Id*. at 31,196.

II. DOMINION'S EFFORTS TO JOIN AN RTO

In furtherance of the Commission's initiatives in Order No. 2000, Dominion attempted, with several other utilities, to develop the Alliance RTO. Ultimately, however, FERC found that the proposed Alliance RTO lacked sufficient geographic scope. *See Alliance Cos*., 97 FERC ¶ 61,327 at 62,529-30 (2001). Nevertheless, consistent with Commission policy, the Commission would "allow recovery of all costs prudently incurred by any Alliance GridCo participant to establish an RTO once it is a member of an RTO." *Alliance Cos*., 99 FERC ¶ 61,105 at 61,442 (2002) (Alliance RTO Order).

Dominion then turned its attention to the already-formed PJM RTO, the operator of the transmission grid in various Mid-Atlantic and Midwestern states. In May 2004, Dominion and PJM filed a joint proposal with the Commission to establish PJM as the RTO for Dominion, under an expansion arrangement to be known as PJM South (the 2004 Filing). *See* JA 5-28. Consistent with Order No.

2000, Dominion would transfer control of its transmission facilities to PJM and PJM would provide service on Dominion's facilities under the PJM tariff. JA 7.

Because Dominion was subject to a Virginia retail rate cap, Dominion would be unable initially to pass through to its Virginia retail customers their allocable share of Dominion's RTO-related costs. JA 12. Dominion requested regulatory asset treatment for these costs, pursuant to which the costs would be recorded as a regulatory asset and amortized once the Virginia retail cap terminated. *Id*. Specifically, Dominion sought FERC approval of its plan to record as a regulatory asset: (1) costs associated with the development of the Alliance RTO; (2) costs associated with integrating with PJM; and (3) PJM administrative fees. JA 22.

III. THE INTEGRATION ORDERS

In *PJM Interconnection, LLC*, 109 FERC ¶ 61,012 (2004) (Integration Order), *on reh'g*, 110 FERC ¶ 61,234 (2005) (Integration Rehearing), the Commission conditionally approved creation of PJM South. The Commission also "approve[d] Dominion's request" for regulatory asset treatment for its RTO-related costs, "subject to the discussion below." Integration Order P 50. As the Commission explained, applicants such as Dominion must incur start-up costs prior to receiving the commercial benefits of being integrated with an RTO. *Id.* When such costs are incurred in periods other than the anticipated benefit period, the costs should be allocated to the periods when the related benefits are expected

to be realized. *Id*. This conclusion is based on the matching principle, which assigns costs to the periods in which benefits are expected to be realized. *Id*. P 50 n.50. The conclusion is not based upon the contention that the costs, if not deferred, would be trapped under retail rate caps. *Id*. Thus, the costs should be initially recorded as an asset, deferred, and then amortized to expense over the anticipated benefit period. *Id*. P 50.

The Commission concluded that Dominion's proposed deferral of its PJM South start-up costs was consistent with this principle. *Id.* P 51. The Commission's Uniform System of Accounts, 18 C.F.R. Part 101, Account 182.3, provides for the booking of costs as a regulatory asset where it is "probable that such items will be included in a different period(s) for purposes of developing rates that the utility is authorized to charge for its utility services." Integration Rehearing P 39. Thus, a utility may recognize a regulatory asset where the utility determines it is probable that a cost that would otherwise be charged to expense in one period will be recovered in rates in another. *Id*. P 41.

The Commission found that Dominion must in the first instance determine whether the costs it proposed to defer met the standard for regulatory assets. Integration Order P 54. If, "based on such assessment, Dominion determines that it is probable that these costs will be recovered in rates in future periods, it should record a regulatory asset for such amounts." *Id*. The Commission made no

findings regarding the ultimate recovery of the deferred costs in Dominion's wholesale rates. Integration Rehearing P 38.

The Virginia Parties petitioned for appellate review of the Integration Orders, but the D.C. Circuit dismissed the petitions for review for lack of aggrievement. *Virginia State Corp. Comm'n v. FERC*, 468 F.3d 845 (D.C. Cir. 2006). The Integration Orders addressed only the proposed accounting treatment of Dominion's RTO-related costs, and did not address or decide the issue of whether the costs ultimately would be recoverable in Dominion's wholesale rates. *Id*. at 847. Because accounting practices are not controlling for ratemaking purposes, there was no rate impact on the Virginia Parties that could constitute the requisite injury-in-fact for standing. *Id*.

In October 2004, PJM and Dominion submitted proposed rates and related revisions to the PJM operating agreements for the purpose of integrating Dominion into PJM. *PJM Interconnection L.L.C. and Virginia Electric and Power Co*., 109 FERC ¶ 61,302 P 1 (2004). Among the proposals was a crediting mechanism designed to facilitate Dominion's deferral of its RTO-related administrative fees. *Id*. P 5. The Commission denied protests regarding the credit mechanism, affirming that the Commission had accepted Dominion's regulatory asset treatment for PJM administrative costs in the Integration Order. *Id*. P 24 (citing Integration Order PP 47-54). However, "[t]he [Integration] Order, although accepting

regulatory asset treatment for these costs, did not determine whether these costs are recoverable in a future rate case." *Id*. (citing Integration Order P 54).

IV. THE ORDERS UNDER REVIEW

A. The Tariff Order

In anticipation of the expiration of the Virginia retail rate cap, in September 2008, Dominion submitted a proposed Deferral Recovery Charge (the 2008 Filing) to recover the RTO costs Dominion had previously deferred pursuant to the Integration Orders. Tariff Order P 1, JA 181. These deferred RTO costs represented the share of Dominion's total RTO-related costs allocable to Dominion's Virginia retail customers. 2008 Filing Exh. DVP-1 at 4, 12, JA 49, 57. The costs were incurred in connection with: (i) efforts to establish the Alliance RTO ($17.8 million); (ii) efforts to join the PJM RTO ($32.9 million); and (iii) deferred PJM administrative fee costs, dating from Dominion's entry into the PJM RTO in May 2005 through August 31, 2009 ($102.5 million). *Id*. P 2, JA 181-82.

The Commission accepted the proposed Deferral Recovery Charge. *Id*. P 27, JA 190. The costs Dominion sought to recover were fully-supported wholesale costs subject to Commission jurisdiction that were fundamentally related to Dominion's efforts to join and participate in an RTO. *Id*. PP 27-28, JA 190-91. In Order No. 2000, recognizing the role that RTOs can play in the development of fully competitive electricity markets, the Commission sought to encourage RTO

formation and participation. *Id*. Because efforts to create RTOs are in furtherance of Commission policies, the Commission permits transmission owners to recover through special surcharges their costs in seeking to form and join an RTO, as well as their ongoing RTO administrative fee costs. *Id*. Here, Dominion sufficiently demonstrated both the nature of the costs and how they were incurred in furtherance of its RTO commitments. *Id*. P 28, JA 191. The prudence of the costs was not challenged. *Id*. Thus, recovery of the costs on an amortized basis through the proposed Deferral Recovery Charge was appropriate. *Id*. PP 28, 30, JA 191.

The Commission rejected arguments that Dominion must be denied recovery because it failed to seek recovery earlier. *Id*. P 29, JA 191. Commission policy at the time Dominion incurred its Alliance RTO formation costs, and at the time that Dominion joined PJM, required deferral of RTO formation costs until Dominion joined an RTO. *Id*. Dominion was not required to file to recover its RTO formation costs at any particular time thereafter. *Id*. No harm had been shown to wholesale customers as a result of the delay. *Id*. P 30, JA 192.

The Commission found no need to address arguments regarding the effect of the Virginia retail rate freeze on retail rate recovery of these costs. *Id*. P 32, JA 193. The Commission found only that Dominion's costs, as filed, were properly recoverable wholesale costs. *Id*. The Commission left for Virginia state regulators

the issue of whether or under which circumstances these costs may be recovered in Dominion's retail rates. *Id*.

B. The Virginia Parties' Requests for Rehearing

On rehearing, the Virginia Consumer Counsel argued, as relevant here, that the Commission erred in approving the Deferral Recovery Charge by: (1) failing to analyze whether Dominion received revenues sufficient to cover these costs during the retail rate freeze, Request for Rehearing and Clarification of the Attorney General of Virginia, Division of Consumer Counsel (Virginia Consumer Counsel Rehearing) at 7, JA 203; and (2) engaging in retroactive ratemaking, because the Tariff Order adjusts prospective rates to make up for an alleged shortfall in prior rates. *Id*. at 11-12, JA 207-08. The Virginia Consumer Counsel also argued accounting error in the Commission's failure to require that Dominion show a regulatory barrier precluded recovery of the RTO costs at the time they were incurred, in order to satisfy the regulatory asset standard. *Id*. at 15-18, JA 211-14.

For its part, the Virginia State Corporation Commission separately argued that the Commission should have required evidence that Dominion's costs were unrecoverable when incurred, Request for Rehearing of the Virginia State Corporation Commission at 3-7, JA 235-39, and that Dominion could not make such a showing. *Id.* at 7-8, JA 239-40.

C. The Rehearing Order

The Commission denied rehearing. Rehearing Order P 1, JA 243. The Commission's long-standing policy is to promote RTO formation and, consistent with this policy, to permit utilities to recover their prudently-incurred RTO formation costs. *Id*. PP 19, 38, JA 249, 258. These costs are an investment in a more efficient method of buying and selling electricity with benefits that accrue to wholesale ratepayers into the future. *Id*. PP 19, 23-24, JA 249, 251-52. Because this investment has future benefits, the Commission amortizes this investment over a number of years (over a 10-year period in the case of Dominion). *Id*. PP 19, 23-24, JA 249, 251-52. *See also id*. P 21, JA 250 (quoting Integration Order P 50). Dominion's costs were wholesale costs subject to FERC jurisdiction that were prudently incurred, attributable to Dominion's commitment to join an RTO (the policy warranting deferred cost treatment), and appropriately allocated to the ratepayers responsible for these costs under the amortization schedule Dominion proposed in its filing. *Id*. P 27, JA 253 (citing Tariff Order PP 28, 30).

The Virginia Parties' rehearing arguments reflect a fundamental misunderstanding of the meaning and function of regulatory assets under the Commission's accounting regulations and the relationship between these regulatory assets and the Commission's ratemaking rules. *Id*. P 20, JA 249. Regulatory assets are defined in the Commission's regulations as "specific

revenues, expenses, gains, or losses that would have been included in net income determination in one period under the general requirements of the Uniform System of Accounts but for it being probable: A. that such items will be included in a different period(s) for purposes of developing the rates the utility is authorized to charge for its utility services." *Id.*, JA 250 (quoting 18 C.F.R. Part 101).

Regulatory asset costs therefore include non-recurring costs that a utility determines are probable of recovery in periods other than the period in which they are incurred. *Id*. P 22, JA 251. Under Commission policy, RTO-related costs are deferred at least until the utility joins an RTO. *Id*. PP 19, 29, JA 249, 254. Commission regulations do not require that deferred costs must be recovered within any specific time period after a utility joins an RTO. *Id*. PP 22, 26, 29, JA 251, 252, 254. Permitting recovery to begin within a few years of Dominion joining the RTO appropriately matched costs with benefits and did not cause harm to wholesale customers. *Id*. PP 26, 29, JA 252-53.

The Commission rejected, as a misinterpretation of Commission policy, arguments that Dominion must show that a regulatory barrier prevented the costs from being recovered in Dominion's retail rates to satisfy the Commission's regulatory asset accounting standard. *Id*. PP 25, 30, JA 252, 254. Rather, a cost incurred to benefit future periods that has not been included in determining the utility's currently effective rates -- *i.e*. the cost is not being recovered in current

rates -- should be amortized over the period in which the benefits are realized. *Id*. Cost recovery at wholesale should not depend on cost recovery at retail. *Id*. PP 30-31, JA 254-55. Dominion was not therefore required to demonstrate that a regulatory barrier barred recovery of these costs in its retail rates. *Id*. P 49, JA 261.

The Commission also rejected the argument that Dominion is being permitted to double-recover costs. *Id*. P 36, JA 257. The Virginia Consumer Counsel provides no evidence that Dominion will recover these costs twice. *Id*. The costs have been accumulated in the regulatory asset account and will be recovered at wholesale through rates on an amortized basis. *Id*. In any event, any issue of double recovery at the retail level is for the state regulator to determine, as the Commission does not regulate retail rates. *Id*.

The Commission further rejected arguments that it had engaged in retroactive ratemaking. *Id*. P 41, JA 258. The rule against retroactive ratemaking prevents a utility from recovering in current rates costs incurred in providing service in prior periods. *Id*. The RTO costs for which the Commission permitted recovery were not costs incurred in providing a past service, but rather were costs incurred to improve the efficiency of service through joining an RTO. *Id*., JA 259. Dominion's RTO investments therefore were properly allocated to the current and future wholesale customers of Dominion. *Id*. P 41, JA 259.

Further, Order No. 2000 put all parties on notice at the outset that RTO start-up costs would be recoverable in transmission rates, and the Alliance RTO Order (*Alliance Cos.*, 99 FERC ¶ 61,105 at 61,442 (2002)) and Dominion's May 11, 2004 filing later provided notice that these costs would be deferred for later recovery. *Id*. P 42, JA 259. Retroactive ratemaking does not apply when customers are on notice that rates may be increased. *Id*. (citing *Columbia Gas Transmission Corp. v. FERC*, 895 F.2d 791, 797 (D.C. Cir. 1990)).

SUMMARY OF ARGUMENT

In the challenged orders, the Commission accepted Dominion's proposed Deferral Recovery Charge, designed to recover Dominion's costs of joining and participating in a Regional Transmission Organization. The costs at issue were wholesale costs, subject to FERC jurisdiction, that were fundamentally related to Dominion's efforts to participate in an RTO. Under Commission policy, recognizing the role that RTOs play in the development of competitive, regional electricity markets, the Commission permits transmission owners such as Dominion to recover through special surcharges their costs in seeking to join an RTO, as well as their ongoing administrative fees related to their participation in the RTO. Further, deferred recovery of Dominion's costs was appropriate, as the costs will be recovered during the period that consumers are receiving the benefits of Dominion's joining an RTO.

Before the Commission, the Virginia Parties asserted that granting recovery of *all* of Dominion's RTO costs constituted retroactive ratemaking. Before this Court, the Virginia Parties now agree with the Commission that RTO start-up costs benefit current and future ratepayers, and therefore approval of those costs does not constitute retroactive ratemaking. Now, the Virginia Parties contend only that approval of Dominion's RTO administrative costs constitute retroactive ratemaking, as those costs provide only past benefits. This argument is

jurisdictionally barred as the Virginia Parties failed to argue before the Commission on rehearing any distinction between RTO start-up costs and RTO administrative costs. In any event, the Commission reasonably concluded that all of Dominion's RTO costs provided current and future ratepayer benefits, and were properly allocated to Dominion's current and future ratepayers.

The Virginia Parties also recognize that no issue of retroactive ratemaking arises if ratepayers are on notice that they may be assessed a surcharge. As the Commission found, Order No. 2000, the Alliance RTO Order, and Dominion's 2004 Filing sufficed to provide notice to ratepayers that Dominion was deferring its RTO costs in expectation of future collection, and that the Commission had a policy of permitting recovery of such costs. While the Virginia Parties assert that no notice was provided of RTO administrative costs, as distinct from start-up costs, this argument is barred because no purported distinction between RTO start-up and administrative costs was presented to the Commission on rehearing. In any event, Dominion's 2004 Filing requesting regulatory asset treatment expressly included RTO administrative costs, which, coupled with the Commission's approval of the accounting treatment in the Integration Orders, and policy of permitting recovery of RTO costs, provided ample notice to ratepayers.

The Virginia Parties also argue that Dominion should have been required to provide evidence that it did not and could not have recovered these RTO costs in

its retail rates when the costs were incurred. The Commission, however, lacks jurisdiction over issues of retail rate recovery under state law. Issues of retail rate recovery are not germane to a determination of whether these costs properly were recoverable in Dominion's FERC-jurisdictional wholesale rates. Dominion amply fulfilled the FPA burden of proof to recover these costs at wholesale. Also, the Virginia Parties provided no evidence of any double recovery under Dominion's retail rates, which were frozen under a retail rate cap prior to any RTO costs being incurred and thus did not include any of the RTO costs in the rate design.

Arguments that the Commission's regulatory asset accounting standard required evidence of Dominion's retail rate recovery fare no better. Accounting practices are not controlling for ratemaking purposes. Further, the Virginia Parties misinterpreted the Commission's standard, which does not require consideration of retail rate recovery to permit deferral of wholesale costs as regulatory assets.

ARGUMENT

I. STANDARD OF REVIEW

Judicial review of FERC orders is governed by FPA § 313(b), 16 U.S.C. § 825*l*(b), which provides that "the findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive." *Sugarloaf Citizens Ass'n v. FERC*, 959 F.2d 508, 512 (4th Cir. 1992). Thus, the scope of the Court's review of FERC action is narrow. *Appomattox River Water Authority v. FERC*, 736 F.2d 1000, 1002 (4th Cir. 1984); *Consolidated Gas Supply Corp. v. FERC*, 653 F.2d 129, 133 (4th Cir. 1981). "This Court may set aside the FERC's order only if we find it to be arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law, or unsupported by substantial evidence." *Appomattox River*, 736 F.2d at 1002 (citations omitted). In addition, the Court "must defer to the Commission's regulatory expertise." *Consolidated Gas*, 653 F.2d at 133. Where Congress has entrusted regulation to the Commission, "[a] presumption of validity . . . attaches to each exercise of the Commission's expertise." *Atlantic Seaboard Corp. v. FPC*, 397 F.2d 753, 755 (4th Cir. 1968). *See also Central Electric Power Coop., Inc. v. Southeastern Power Administration*, 338 F.3d 333, 337 (4th Cir. 2003) ("Given the expertise of agencies in the fields they regulate, a presumption of regularity attaches to administrative actions.").

"'Statutory reasonableness is an abstract quality represented by an area rather than a pinpoint.'" *Consolidated Gas*, 653 F.2d at 134 (quoting *Montana-Dakota Utils. Co. v. Northwestern Public Serv. Co*., 341 U.S. 246, 251 (1951)). "The statutory requirement that rates be 'just and reasonable' is obviously incapable of precise judicial definition, and [the Court] afford[s] great deference to the Commission in its rate decisions." *Morgan Stanley*, 128 S. Ct. at 2738. "Because [i]ssues of rate design are fairly technical, and, insofar as they are not technical, involve policy judgments that lie at the core of the regulatory mission, [the court's] review of whether a particular rate design is just and reasonable is highly deferential." *Northern States Power Co. v. FERC*, 30 F.3d 177, 180 (D.C. Cir. 1994) (internal quotation marks and citations omitted).

II. THE COMMISSION REASONABLY APPROVED DOMINION'S DEFERRAL RECOVERY CHARGE.

A. Commission Policy Permits Recovery Of RTO-Related Costs In FERC-Jurisdictional Wholesale Rates.

In its Order No. 2000 rulemaking, the Commission held that RTOs could successfully address the existing impediments to efficient and competitive grid operation and that substantial cost savings were likely to result from the formation of RTOs. Rehearing Order P 38, JA 257-58 (citing Order No. 2000 at 30,993). *See also* Tariff Order P 27, JA 190. The Commission's long-standing policy is to promote the formation of Regional Transmission Organizations, and, consistent

with this policy, to permit utilities to recover their prudently-incurred RTO formation costs. Rehearing Order PP 19, 38, JA 249, 258. Order No. 2000 "assure[d] utilities that they will not be penalized for RTO participation," Order No. 2000 at 31,172, and clarified that "the reasonable costs of developing an RTO may be included in transmission rates." *Id*. at 31,196.

Because efforts to create RTOs further Commission policies, the Commission permits transmission owners to recover their costs in seeking to form and join an RTO, as well as their ongoing administrative fee costs related to their participation in the RTO. Rehearing Order P 23, JA 251; Tariff Order P 27, JA 190. These costs are an investment in a more efficient method of buying and selling electricity, with benefits that accrue to wholesale ratepayers into the future, in periods after the costs are incurred. Rehearing Order PP 19, 23, JA 249, 251. Because this investment has future benefits to the wholesale ratepayers who participate in the RTO, the Commission amortizes this investment over a number of years. Rehearing Order P 19, JA 249. *See also id*. P 21, JA 250 (quoting Integration Order P 50).

In the 2008 Filing, Dominion sought to recover RTO costs incurred in connection with: (i) early unsuccessful efforts to establish the Alliance RTO; (ii) later successful efforts to join the PJM RTO; and (iii) PJM administrative fees,

dating from Dominion's entry into the PJM RTO in May 2005 through August 31, 2009. Tariff Order P 2, JA 181-82; 2008 Filing Exh. DVP-1 at 17, JA 62.

The Commission found that Dominion's costs, including its ongoing administrative costs, were fully-supported costs related to Dominion's initially-failed but ultimately successful effort to join an RTO. Tariff Order P 28, JA 191. These costs were appropriately recovered as they were prudently incurred, attributable to Dominion's commitment to join an RTO (the policy warranting deferred cost treatment), and appropriately allocated to the ratepayers responsible for (and benefitting from) these costs under the amortization schedule Dominion proposed in its filing. Rehearing Order PP 24, 27, JA 252-53 (citing Tariff Order PP 28, 30, JA 191).

B. The Commission's Approval Of The Deferral Recovery Charge Did Not Constitute Retroactive Ratemaking.

1. The Deferral Recovery Charge Appropriately Matches The Costs And Benefits Of RTO Participation.

The Virginia Parties generally suggest that, because "the RTO costs Dominion seeks to recover were incurred in the past," allowing recovery of these costs constitutes retroactive ratemaking. Br. 3, 24-25. However, the rule against retroactive ratemaking prevents a utility from recovering in current rates costs incurred in providing service in prior periods. Rehearing Order P 41, JA 259. Here, the subject RTO costs were not incurred in providing a past service, but

rather were costs incurred to improve the efficiency of service through joining an RTO, with benefits accruing to wholesale ratepayers into the future. *Id*. at PP 19, 23, 41, JA 249, 251, 259. *See, e.g*., *Midwest ISO Transmission Owners*, 373 F.3d at 1371 (the benefits of regional entities, such as an overall reduction in the cost of transmitting energy within the region and large scale regional coordination and planning of transmission, redound to all users of the grid, and therefore are properly allocable to all users of the grid); *East Kentucky Power Cooperative, Inc. v. FERC*, 489 F.3d 1299, 1307 (D.C. Cir. 2007) (the Independent System Operator's costs of operating the regional grid may reasonably be assessed on all transmission loads delivered under the grid "because the benefits of an ISO flow to all who transact on the grid."); *Western Area Power Administration v. FERC*, 525 F.3d 40, 54 (D.C. Cir. 2008) (regional transmission entities such as the one in California generate significant benefits for all customers of a transmission system).

Because the benefits of RTO participation are enjoyed by current and future ratepayers, Dominion's RTO investments properly are allocated to Dominion's current and future wholesale ratepayers, notwithstanding that the costs were themselves incurred in the past. Rehearing Order P 41, JA 259 (citing *Public Systems v. FERC*, 709 F.2d 73, 85 (D.C. Cir. 1983) (retroactive ratemaking not implicated when the Commission attributes costs to those that benefit from cost incurrence)).

> To some degree, all utility rates reflect past costs; utilities typically expend funds today (for example, constructing generation facilities), fully expecting to recover those costs through future rates. In fact, current rates often include past costs that utilities deferred in order to avoid rate increases. Cost causation requires not that costs be incurred at the same time they are included in rates, but that the rates "reflect to some degree the costs actually caused by the customer who must pay them."

Transmission Access Policy Study Group v. FERC, 225 F.3d 667, 708 (D.C. Cir. 2000) (quoting *KN Energy, Inc. v. FERC*, 968 F.2d 1295, 1300 (D.C. Cir. 1992)), *aff'd sub. nom, New York v. FERC*, 535 U.S. 1 (2002).

Thus, the Commission reasonably permitted deferred recovery of Dominion's RTO costs because those costs are designed to produce efficiency benefits to future ratepayers. Rehearing Order PP 19, 21, JA 249, 250. *See Western Resources, Inc. v. FERC*, 72 F.3d 147, 152 (D.C. Cir. 1995) (where customers would receive current and future benefits from transition to a competitive natural gas market, "take or pay" costs resulting from transition were properly allocated to current and future rate periods); *Public Systems*, 709 F.2d at 85 (no retroactive ratemaking where provision permitting utilities to "make up" deficiencies in their deferred tax reserves resulting from a change in tax treatment spread the burden fairly among future ratepayer generations).

The Commission further reasonably determined that permitting recovery of RTO costs within a few years of Dominion joining the RTO appropriately matched costs with benefits and caused no harm to wholesale customers. *Id*. P 26, JA 252.

Dominion's RTO costs "will be recovered during the period in which consumers are receiving the benefits of Dominion's joining PJM." *Id*. P 43, JA 260. The cost causation principle does not require allocation of costs with "'exacting precision.'" *Public Serv. Comm'n of Wisconsin v. FERC*, 545 F.3d 1058, 1067 (D.C. Cir. 2008) (quoting *Midwest ISO Transmission Owners*, 373 F.3d at 1369). Rather, it simply requires "'that all approved rates reflect *to some degree* the costs actually caused by the customer who must pay them.'" *Public Serv. Comm'n*, 545 F.3d at 1067 (quoting *Midwest ISO Transmission Owners*, 373 F.3d at 1368). *See also Transmission Access Policy Study Group*, 225 F.3d at 708 (same); *KN Energy*, 968 F.2d at 1300 (same); *Sithe/Independence Power Partners, L.P. v. FERC*, 285 F.3d 1, 5 (D.C. Cir. 2002) ("FERC is not bound to reject any rate mechanism that tracks the cost-causation principle less than perfectly.")

2. The Virginia Parties Concede That RTO Start-Up Costs Match Costs And Benefits, And Their Distinction Between RTO Start-Up Costs And RTO Administrative Fees Is Jurisdictionally Barred And Without Merit.

The Virginia Parties "do not challenge" that "retroactive ratemaking is not implicated when costs incurred in the past provide future benefits." *See* Br. 25-26. The Virginia Parties agree with the Commission that, where costs and benefits are matched, the recovery "constitutes an allocation of costs rather than an attempt to recoup asserted shortfalls under prior rates." *Id*. at 26. The Virginia Parties also agree that RTO "start-up" and "development" costs provide benefits beyond the

period for which those costs are incurred, and therefore permitting recovery of such costs does not constitute retroactive ratemaking. *Id*. at 26-27. *See also* Br. 32 ("As discussed above, RTO development, or start-up, costs provide a future benefit and therefore may not implicate the rule against retroactive ratemaking"). Thus, the Virginia Parties now agree with the Commission that the deferred recovery of RTO start-up costs does not constitute retroactive ratemaking.

The Virginia Parties now assert on brief, however, that Dominion's PJM RTO administrative fees – unlike its RTO start-up costs -- are fees for past services that provide no future benefit, and therefore their rate recovery constitutes retroactive ratemaking. Br. 26-27, 32. The Virginia Parties rely on P 52 of the Integration Order (discussing general accounting of RTO costs) to support this proposition. Br. 27.

The Court lacks jurisdiction to consider this new argument because it was never raised before the Commission on rehearing. As this Court has recognized, its review of FERC orders "is limited by 16 U.S.C. § 825*l*, which provides, 'No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure to do so.'" *Mt. Lookout-Mt. Nebo Property Protection Ass'n v. FERC*, 143 F.3d 165, 173 (4th Cir. 1998) (citing *Escondido Mut. Water Co. v. La Jolla Band of Mission Indians*, 466 U.S.

765, 779 n.23 (1984) (where licensees did not raise an argument in their petition for rehearing before FERC, they may not raise the argument before the Court)). *See also County of Halifax v. Lever*, 718 F.2d 649, 653 (4th Cir. 1983) (same). The Court "will not consider a contention not presented to, or considered by, the Commission." *Aquenergy Systems, Inc. v. FERC*, 857 F.2d 227, 230 (4th Cir. 1988). *See also Consolidated Gas Supply Corp. v. FERC*, 611 F.2d 951, 958-59 (4th Cir. 1979) (refusing to consider "the two grounds most strenuously urged" by petitioner where they were never raised to the Commission on rehearing).

On rehearing before the Commission, the Virginia Consumer Counsel argued that the Commission's approval of *all* of Dominion's requested RTO costs (RTO start-up costs *and* RTO administrative costs) constituted unlawful retroactive ratemaking because it allowed Dominion to adjust future rates to make up for a shortfall in prior rates. *See* Virginia Consumer Counsel Request for Rehearing at 11-12, JA 207-08.[2] Indeed, the Virginia Consumer Counsel Rehearing Request refers throughout the pleading to all of Dominion's costs collectively as "RTO costs," with no differentiation between start-up and administrative costs. *See id*. n. 1, JA 197. The rehearing request made no suggestion whatever that the rate treatment of RTO start-up costs was or should be in any way distinguishable from

[2] The Virginia State Corporation Commission's Request for Rehearing (found at JA 233-41) made no argument regarding retroactive ratemaking.

the treatment of RTO administrative costs. Nor did the rehearing request cite to P 52 of the Integration Order, on which the Virginia Parties now rely. Br. 27.

In effect, in their brief before this Court, the Virginia Parties are arguing for a different result than that urged before the Commission. Before the Commission, the Virginia Consumer Counsel sought to bar recovery of *all* Dominion deferred RTO costs as retroactive ratemaking, whereas before this Court the Virginia Parties now concede that recovery of RTO start-up costs is not retroactive ratemaking, but assert that recovery of RTO administrative costs is retroactive ratemaking. *See* Br. 27 (arguing it is arbitrary and capricious for FERC to approve recovery of *all* RTO costs when only *some* of those costs, RTO start-up costs, benefitted future periods). As the Virginia Parties never argued to the Commission this alternative result – part of the costs are recoverable and part not – the Virginia Parties are jurisdictionally barred from raising it now. Having failed to assert a distinction between RTO start-up costs and administrative costs on rehearing, the Virginia Parties cannot now be heard to argue that the Commission erred in failing to make that distinction.

Further, the Virginia Parties incorrectly assert that the Commission found only that RTO start-up costs provide future benefits, and made no finding with regard to administrative costs. Br. 26-27 (quoting Rehearing Order P 41, JA 258). To the contrary, the Commission found that all of Dominion's costs – start-up and

administrative – provided current and future benefits, and were properly allocable to current and future ratepayers. "The costs Dominion proposes to recover here, including its ongoing administrative fee costs, are related to its initially-failed but ultimately successful effort to joint an RTO." Tariff Order P 28, JA 191. The Commission specifically permits recovery through special surcharges of both start-up and administrative costs, Tariff Order P 27, JA 190; Rehearing Order P 23, JA 251, and the Commission has not required that any of these costs be recovered within any specific time period. Rehearing Order P 29, JA 254. All of Dominion's costs "will be recovered during the period in which consumers are receiving the benefits of Dominion's joining PJM." Rehearing Order P 43, JA 260. Thus, all of Dominion's costs were "attributable to Dominion's commitment to join an RTO (the policy warranting deferred cost treatment), and appropriately allocated to ratepayers responsible for these costs under the amortization schedule Dominion proposed in its filing." Rehearing Order P 27, JA 253. *See, e.g., Midwest ISO Transmission Owners*, 373 F.3d at 1371 (the administrative costs of having a regional transmission entity are appropriately recoverable from all users of the system).

Integration Order P 52 is not to the contrary. Br. 27. Paragraphs 51 and 52 of the Integration Order explained when RTO costs are recognized for purposes of general accounting requirements: deferred start-up costs begin amortization on the

date the transmission owner is integrated into the RTO (P 51) and administrative fees are charged to expense in the period when incurred (P 52). However, P 53 explained that, "notwithstanding the general accounting requirements for RTO related costs" discussed in PP 51 and 52, the Commission's Uniform System of Accounts also provides for recognition of regulatory assets. Integration Order P 53. If costs are treated as a regulatory asset, rate recovery is provided "in periods other than the period [the costs] would otherwise be charged to expense under the general accounting requirements for costs." *Id*. P 54.

In other words, a regulatory asset is by definition an amount that is being charged in a period other than the one in which it would ordinarily be expensed. Integration Order P 52 describes when administrative fees would *ordinarily* be expensed, but PP 53 and 54 explain that regulatory asset treatment permits recovery in other periods. *See* Br. 9 (citing Integration Order P 50 as stating that "[t]he costs of providing regulated electric service will normally be expensed in the period in which they are incurred or, under certain circumstances (as in the case for regulatory assets), 'deferred and then amortized to expense over the anticipated benefit period'"). Thus, Integration Order P 52 does not support a finding that RTO administrative costs are unrecoverable in periods after they are incurred.

Indeed, the Rehearing Order expressly stated that P 52 of the Integration Order was not properly interpreted to require that utilities file for rate recovery

immediately upon joining the RTO. Rehearing Order P 26, JA 252 (citing Integration Order P 52). To the contrary, there is no such requirement in the Commission's regulations or policy. *Id*. Rather, the Commission has not required that such costs be recovered within any specific time period after the utility joins an RTO. *Id*. PP 22, 25, 29, JA 251, 252, 254.

3. Ratepayers Had Ample Notice That Dominion Sought Deferred Recovery Of Costs Generally Allowed By The Commission.

The Virginia Parties also recognize that rates are not retroactive where ratepayers are on notice that the costs in question may be subject to future recovery. Br. 29. *See* Rehearing Order P 42, JA 259 (retroactive ratemaking does not apply when the customers are on notice that rates may be increased) (citing *Columbia Gas*, 895 F.2d at 797 (notice does not relieve the Commission from the prohibition against retroactive ratemaking but, instead, "changes what would be purely retroactive ratemaking into a functionally prospective process")). *See also Natural Gas Clearinghouse v. FERC*, 965 F.2d 1066, 1075 (D.C. Cir. 1992) (same).

Ratepayers had ample notice here. Rehearing Order P 42, JA 259. Order No. 2000 put all parties on notice at the outset that RTO costs would be recoverable in transmission rates. *Id*. Order No. 2000 expressly "assure[d] utilities that they will not be penalized for RTO participation," Order No. 2000 at 31,172,

and clarified that "the reasonable costs of developing an RTO may be included in transmission rates." *Id*. at 31,196. Such statements provide broad notice of a policy to hold utilities harmless for the costs of RTO participation.

Transwestern Pipeline Co. v. FERC, 897 F.2d 570, 580 (D.C. Cir. 1990) (cited Br. 29), is not to the contrary. In *Transwestern*, the preamble to FERC regulations stated a general policy of assuring pipeline recovery of all purchased gas costs, but a regulation specifically provided that customers leaving a pipeline were no longer responsible for purchased gas adjustments. *Id*. at 580. In light of the regulation, pipeline customers were not on notice that their purchased gas adjustment balances would follow them if the pipeline's purchased gas adjustment program ended. *Id*. Here, no contrary language in regulations or anywhere else contradicts the Commission's express policy of compensating transmission owners for the costs of participating in an RTO.

The Alliance RTO Order and Dominion's 2004 Filing further provided notice that Dominion's RTO costs would be deferred for later recovery. Rehearing Order P 42, JA 259. The Alliance RTO Order, 99 FERC at 61,442, stated that the Commission would allow recovery of "all costs prudently incurred by any Alliance GridCo participant to establish an RTO once it is a member of an RTO." Thus, the Commission specifically required deferral of the costs incurred in attempting to form the Alliance RTO, until the transmission owners that had incurred these costs

became members of a Commission-approved RTO. Tariff Order P 27, JA 190; Rehearing Order P 19, JA 249.

Dominion's 2004 Filing, moreover, provided notice that Dominion intended to defer its PJM RTO start-up and administrative costs, as well as the Alliance start-up costs, for later collection following termination of the Virginia retail rate cap. Rehearing Order P 42, JA 259. As Dominion explained at the time of its filing:

> Dominion requests that the Commission authorize for deferral as a regulatory asset all costs incurred by Dominion and its affiliate during the period of June 1, 1998 to May 1, 2003 related to the establishment of the Alliance RTO. Dominion will also incur, for the period of December 21, 2001 to the end of the state imposed rate cap, expenditures related to the establishment and operation of PJM South. Dominion respectfully requests that the Commission authorize Dominion to capture and defer the aforementioned expenditures as a regulatory asset until the existing Virginia retail rate cap ends.

2004 Filing, JA 22. Dominion expressly requested deferral of: (1) costs associated with developing the Alliance RTO; (2) costs associated with integrating with PJM and (3) PJM administrative fees. *Id*. *See* Br. 9 (Dominion's 2004 Filing sought regulatory asset treatment for Alliance and PJM start-up costs and PJM administrative fees).

In the Integration Order, the Commission found that Dominion may give its RTO start-up costs and administrative fees regulatory asset treatment, provided that Dominion first determines that these costs qualify for such treatment, and the

Commission would determine in a future rate case whether the deferred costs were recoverable. Tariff Order P 5, JA 182 (citing Integration Order PP 53-54). *See also PJM Interconnection, L.L.C.*, 109 FERC ¶ 61,302 P 24 (2004) (stating that, in the Integration Order, "the Commission accepted Dominion's proposal to provide for regulatory asset treatment for PJM administrative costs"). Thus, following the Alliance RTO Order and Dominion's 2004 Filing, ratepayers had ample notice that the Alliance start-up costs, and the PJM start-up costs and administrative costs, would be deferred in the expectation of future recovery.

4. The Virginia Parties' Attempts To Discount The Notice Provided Are Unavailing.

The Virginia Parties complain that Order No. 2000 and the Alliance RTO Order gave notice only of the costs of "developing" or "establishing" an RTO, and did not give notice that administrative fees would also be recovered. Br. 29. As discussed previously, however, any argument that the Commission erred in failing to distinguish between RTO start-up costs and administrative costs is jurisdictionally barred as the Virginia Parties failed to argue on rehearing before the Commission that administrative costs were a separate category – to be treated differently – from RTO start-up costs. *See supra,* Argument Section II(B)(2). As no argument was made that administrative costs were or should be separable from start-up costs for purposes of rate recovery, the Virginia Parties are jurisdictionally barred now from arguing that the Commission erred in failing to require specific

notice that such administrative costs – as distinct from start-up costs – would be subject to future collection.

Further, Dominion did not begin to incur PJM administrative costs until May 2005. *See* 2008 Filing Exh. DVP-1 at 17, JA 62. Prior to that time, Dominion had already made its 2004 Filing seeking deferred rate treatment for RTO costs *expressly including the PJM administrative costs*, and the Commission had accepted such accounting treatment. Integration Order PP 53-54 (October 5, 2004); *PJM Interconnection, L.L.C.*, 109 FERC ¶ 61,302 P 24 (Dec. 21, 2004); Integration Rehearing P 29 (March 4, 2005).

The Virginia Parties assert that notice must come from the Commission, and therefore Dominion's 2004 Filing cannot suffice to provide notice that Dominion's RTO costs would be deferred and may be subject to later recovery. Br. at 31, citing *Columbia Gas*, 895 F.2d at 797, and *OXY USA, Inc. v. FERC*, 64 F.3d 679, (D.C. Cir. 1995), for the proposition that there is no retroactive ratemaking when *the Commission* places parties on notice of potential rate changes.

First, the Virginia Parties disregard the Commission's acceptance of deferred regulatory asset rate treatment for Dominion's RTO costs – including the PJM administrative fees – prior to the time that Dominion began to incur, and to defer, PJM administrative fees. Therefore, the Commission as well as Dominion placed ratepayers on notice that such costs were being deferred for potential future

collection in a Dominion rate filing. *See* Integration Order P 54 (rate recovery of Dominion's deferred costs will be determined in a future rate proceeding); Integration Rehearing P 29 (same); *PJM Interconnection L.L.C.*, 109 FERC ¶ 61,302 P 24 (Commission accepted regulatory asset accounting treatment in the Integration Order, but rate recovery will be determined in a future rate case).

Further, while certainly notice by the Commission suffices to avoid charges of retroactive ratemaking, "notice from FERC is not always required." *Public Utils. Comm'n v. FERC*, 988 F.2d 154, 165 (D.C. Cir. 1993). Rather, sufficient notice of a potential rate change may be provided by the utility's request for a rate action, particularly where the request is made in the context of a Commission policy of granting such requests. *Id.*, 988 F.2d at 165 (notice from pipeline filing seeking additional take-or-pay costs and FERC's policy of permitting recovery of take-or-pay costs); *Natural Gas Clearinghouse*, 965 F.2d at 1075 (notice from pipeline tariff sheets and other filings reserving the right to seek a surcharge if a FERC order were reversed on appeal); *Consolidated Edison Co. v. FERC*, 958 F.2d 429, 434-35 (D.C. Cir. 1992) (notice from pipeline filing requesting a retroactive effective date and FERC's policy of granting such requests); *Louisiana Pub. Serv. Co. v. FERC*, 482 F.3d 510, 520 (D.C. Cir. 2007) (notice from filing of a complaint against a rate). Such notice is sufficient even where ratepayers do not

know whether FERC will grant the rate request. *Public Utils. Comm'n*, 988 F.2d at 165.

Here, Dominion's 2004 Filing requested recovery of deferred RTO costs – including both start-up and administrative costs – and existing Commission policy following Order No. 2000 permitted recovery by transmission owners through special surcharges of their costs in seeking to form and join an RTO, as well as their ongoing administrative costs related to their participation in the RTO. Tariff Order P 27, JA 190 (citing *Idaho Power Co*., 123 FERC ¶ 61,104 P 10 (2008); *Entergy Services, Inc*., 117 FERC ¶ 61,320 (2006); *Illinois Power Co*., 108 FERC ¶ 61,258 (2004); *Alliance Cos*., 99 FERC ¶ 61,105 (2002)); Rehearing Order P 23, JA 251. Prior to the challenged orders, the Commission had permitted deferred recovery of RTO costs past the date that the utility had joined an RTO. Tariff Order P 30, JA 191 (citing *Northeast Utils. Serv. Co*., 121 FERC ¶ 61,308 P 19 (2007) (permitting deferred recovery of RTO costs subject only to an analysis of whether delay in recovery would result in rate impact to wholesale customers); *Northeast Utils. Serv. Co.,* 124 FERC ¶ 61,098 P 19 (2008) (accepting compliance filing showing no rate impact from delay); *Central Maine Power Co*., 116 FERC ¶ 61,129 P 11 (2006) (accepting transmission owner's proposal for rate recovery of deferred RTO formation costs)); Rehearing Order P 29, JA 254. *See also Midwest ISO*, 373 F.3d at 1365, 1371 (permitting regional Midwest transmission operator to

defer recovery of administrative costs exceeding a cap during a six-year transition period until the end of the transition period, and to be repaid on a five-year amortization schedule through a surcharge to all customers). Thus, Dominion's request for deferred rate recovery and the Commission's policy of granting recovery of RTO costs, including deferred costs – both start-up and administrative – constituted sufficient notice of the Deferral Recovery Charge to avoid any issues of retroactive ratemaking.

The Virginia Parties point out that the 2004 Filing only signaled Dominion's intention to seek a future surcharge, and the filed tariff did not itself address the potential surcharge. Br. 31. *See also* Br. 29 (arguing that there was no provisional rate in place that might be changed). A tariff filing reserving the right to impose surcharges is not required in order to avoid retroactive ratemaking. *Canadian Association of Petroleum Producers v. FERC*, 254 F.3d 289, 299 (D.C. Cir. 2001). "So long as the parties had adequate notice that surcharges might be imposed in the future, imposition of surcharges does not violate the filed rate doctrine." *Id*. "'The filed rate doctrine simply does not extend to cases in which buyers are on adequate notice that resolution of some specific issue may cause a later adjustment to the rate being collected at the time of service.'" *Id*. (quoting *Natural Gas Clearinghouse*, 965 F.2d at 1075). In *Canadian Ass'n*, the pipeline's initial rate filing – combined with ongoing litigation and absence of a final, non-appealable

order – provided the necessary notice to shippers. *Id*. Similarly here, Dominion's 2004 Filing and the Commission's Integration Orders, combined with Order No. 2000 and the Alliance RTO Order, provided the necessary notice to ratepayers that Dominion's deferred RTO costs – including administrative fees – may be subject to recovery in a future rate case.

C. The Commission Reasonably Determined That Dominion Was Not Required To Show That The RTO Costs Were Unrecovered Or Unrecoverable In Dominion's Retail Rates.

1. The Commission Reasonably Declined To Consider Retail Rate Recovery Issues As The Commission Lacks Statutory Jurisdiction To Regulate Retail Rates.

The Virginia Parties assert that "FERC's failure to ensure that Dominion's historic RTO costs were not (i) as a factual matter, already recovered or (ii) unrecoverable as a legal matter violates FERC's duty under FPA § 205, [16 U.S.C. § 824d] to set 'just and reasonable' rates." Br. 36. FERC's alleged failure to require "an evidentiary showing that Dominion's retail rates in effect applicable to that period prevented recovery of those costs in that period" purportedly "permits the unlawful double recovery of costs." *Id*. 37.

The Virginia Parties thus would require that the Commission undertake a full rate case inquiry into whether Dominion's retail rate revenues were sufficiently high to cover the RTO costs, *see* Br. 36-39 -- even though the RTO costs were not

included in Dominion's retail rate design.[3] *See* Br. 34-35 (the "prior standard required Dominion to demonstrate the recoveries under 'retail rates' during the historic period when the RTO costs were incurred"); Br. 39 (arguing that an "examination" of Dominion's "overall rate and all cost components" was required). The Virginia Parties also require an inquiry into whether Virginia law presented a regulatory barrier to recovery of the RTO costs at the time they were incurred. Br. 40-41.

The Commission reasonably found it was not required to determine whether the RTO costs were unrecovered or unrecoverable under state law. Tariff Order P 32, JA 193; Rehearing Order P 31, JA 255. The Commission does not regulate retail rates, and the issue of whether these costs were recovered or were recoverable at retail is properly left to the state regulator to determine. Tariff Order P 32, JA 193; Rehearing Order P 36, JA 257.

Accordingly, the Commission made no determinations as to the effect of a retail rate freeze on recovery of previously-incurred wholesale costs. Tariff Order P 32, JA 193; Rehearing Order P 31, JA 256. The Commission determined only that Dominion's costs, as filed, were properly recoverable wholesale costs. Tariff Order P 32, JA 193; Rehearing Order P 31, JA 256. Dominion was not required to

[3] None of the RTO costs at issue were included in Dominion's retail rates because Dominion's retail rates were frozen as of July 1, 1999, before Dominion had incurred any of the RTO costs. 2008 Filing at 3, JA 31; 2008 Filing Exh. DVP-1 at 3, 13, JA 48, 58.

provide evidence of its earnings under its capped retail rates because the issue of rate recovery at retail is not germane to the Commission's consideration of whether wholesale rate recovery is appropriate. Rehearing Order P 49, JA 261. *See also Midwest ISO Transmission Owners*, 373 F.3d at 1372 (state retail considerations "do not circumscribe FERC's authority;" rather, principles of federal preemption and supremacy "operate to prevent the states from taking regulatory action in derogation of federal regulatory objectives"). As the Commission does not regulate retail rates, any issue of double recovery at the retail rate level is a question for the state regulator to determine. Rehearing Order P 36, JA 257.

Moreover, the Virginia Parties provided no evidence that Dominion would recover its RTO costs twice. Rehearing Order P 36, JA 257. The RTO costs at issue were not previously included in designing Dominion's currently effective rates, but rather were accumulated in a regulatory asset account for future recovery. *Id*. PP 25, 36, JA 252, 257; n.3, *supra*. *See also, e.g., Western Area Power Admin*., 525 F.3d at 54 (the benefits produced by regional transmission entities reflect new services not previously provided by utilities, and therefore the cost of the regional entity benefits is not included in pre-existing contract rates); *East Kentucky*, 489 F.3d at 1307 (same). Because the RTO cost categories at issue had never been included in Dominion's rates, there was no basis to believe that these costs were being double-recovered, and the Virginia Parties provided no evidence to the

contrary. Rehearing Order P 36, JA 257. Speculation that Dominion's retail rates may have been sufficient to recover the RTO costs – even though those costs were not included in the rate design – would not in any event suffice as grounds for requiring an evidentiary hearing. *City of Ukiah v. FERC*, 729 F.2d 793, 799 (D.C. Cir. 1984) ("'Mere allegations of disputed facts are insufficient to mandate a hearing; petitioners must make an adequate proffer of evidence to support them.'") (quoting *Cerro Wire & Cable Co. v. FERC*, 677 F.2d 124, 129 (D.C. Cir. 1982)). *See also, e.g., Kansas Power and Light Co. v. FERC*, 851 F.2d 1479, 1484 (D.C. Cir. 1988) (same).

Likewise, the Commission did not determine whether retail rate recovery was precluded under Virginia law during the retail rate freeze period. *See* Br. 40. The question of wholesale recovery of costs does not depend on a determination of whether these costs were recoverable in retail rates. Rehearing Order P 22, PP 30-31, JA 251, 254-55. For example, wholesale costs can appropriately be passed through to transmission owners regardless of whether the transmission owners can pass those costs on to consumers in retail rates. *Id*. P 30, JA 254 (citing *Midwest ISO Transmission Owners*, 373 F.3d at 1372). As the D.C. Circuit recognized, where the Commission's rate recovery authorizations result in trapped costs, the transmission owners' "initial recourse is to their state regulators and contractual partners armed with principles of federal preemption and the Supremacy Clause –

not to FERC." *Id*. (quoting *Midwest ISO Transmission Owners*, 373 F.3d at 1372). As the issue of retail rates is beyond the Commission's statutory authority, the Commission properly declined to decide retail rate issues arising under state law. *Id*. P 50, JA 262.

Because the Commission lacks statutory authority to decide state law retail rate issues, failing to require evidence of retail rate recovery does not "unlawfully sidestep[]" Dominion's burden of proof under the Federal Power Act for rate requests or accounting entries. Br. 37-38. Dominion fully met its statutory burden of proof requirements. Tariff Order P 28, JA 191; Rehearing Order P 48, JA 261. The RTO costs that Dominion proposed to recover, including its ongoing administrative costs, were related to its initially-failed but ultimately successful effort to join an RTO. Tariff Order P 28, JA 191. The costs were fully itemized in Dominion's filing, in prepared testimony, exhibits and supporting work papers. *Id*. Dominion sufficiently demonstrated both the nature of the costs and how they were incurred in furtherance of its RTO commitments. *Id*. Further, the prudence of Dominion's costs was not challenged. *Id*. Accordingly, the Commission found Dominion's costs properly recoverable through the proposed surcharge. *Id*.; Rehearing Order P 48, JA 261.

2. The Regulatory Asset Accounting Standard Does Not Support The Virginia Parties' Claims.

The Virginia Parties assert that FERC's regulatory accounting standard required Dominion to provide evidence of past earnings under its retail rates to obtain rate recovery. Br. 33. This argument fails for a number of reasons.

First, the regulatory asset standard is an accounting standard, which is not controlling for ratemaking purposes. Rehearing Order P 34, JA 256; Tariff Order P 31 n.33, JA 192. As this Court has recognized, "an item may be treated differently for accounting than for ratemaking purposes." *Consolidated Gas Supply Corp. v. FERC*, 653 F.2d 129, 135-36 (4th Cir. 1981). The determination of whether costs are appropriately recoverable is made not by the accounting treatment these costs may have been given, but in a Federal Power Act § 205, 16 U.S.C. § 824d, proceeding in which the applicant seeks to recover the costs in its wholesale rates. Tariff Order P 31, JA 192; Rehearing Order P 22, JA 251. Thus the issue of rate recovery is not whether Dominion could or should have chosen a different account in which to book the costs at issue, but whether these costs are properly recoverable as wholesale costs under the FPA. Tariff Order P 31, JA 192. When Dominion filed to recover its RTO costs, the Commission determined consistent with its precedent that amortization of these costs to future periods was appropriate and consistent with the Commission's treatment of RTO costs. Tariff

Order P 31, JA 192; Rehearing Order P 34, JA 256. *See also* Rehearing Order PP 23, 47-48, JA 251, 261.

Accordingly, whether or not the costs at issue are properly categorized as regulatory assets for accounting purposes does not control the issue of their recoverability, and, therefore, the Virginia Parties' arguments regarding this accounting standard do not address, let alone undermine, the Commission's rate determination regarding recoverability of these costs. For this same reason, the D.C. Circuit dismissed the Virginia Parties' appeal of the Commission's accounting determination in the Integration Orders for failure to show aggrievement, as the accounting treatment provided the RTO costs at issue does not control the question of whether the costs are recoverable in Dominion's rates. *Virginia State Corp. Comm'n*, 468 F.3d at 847.

This point further answers the assertion that the Commission improperly relied on Dominion's belief that the deferred costs would be recoverable. Br. 34. Dominion's subjective belief regarding the future recoverability of rates is relevant only to the issue of whether the RTO costs were properly recorded as regulatory assets, not whether they were properly recoverable in Dominion's wholesale rates. Tariff Order P 31, JA 192; Rehearing Order P 47, JA 261. *See also* Rehearing Order PP 23-24, JA 251-52. The utility in the first instance determines whether a particular cost is likely to be recoverable in future rates and therefore should be

accounted for as a regulatory asset. Rehearing Order P 22, JA 251. *See, e.g., Virginia State Corp. Comm'n*, 468 F.3d at 848 (finding that FERC's Integration Order "calls upon Dominion to assess whether its start-up costs meet the requirements of a regulatory asset"). This initial determination can be made by the utility's accountants and auditors, without prior Commission approval. Rehearing Order P 34, JA 256 (citing Integration Order P 40). If the utility determines that the cost is not included in existing rates and it is probable that such cost will be included in future rates it can book the cost as a regulatory asset. *Id*. P 22, JA 251.

Here, Dominion chose to treat these RTO costs as a regulatory asset because it believed that Commission policy permitted recovery of such costs in wholesale rates in later periods. *Id*. P 23, JA 251. Dominion's subjective belief as to recoverability thus was only relevant to the finding that Dominion properly booked the costs as regulatory assets; *i.e*., the Commission found that the costs were properly booked as regulatory assets because Dominion had a reasonable expectation that its RTO investments could be recovered in future periods. Tariff Order P 31, JA 192; Rehearing Order P 47, JA 261. *See also* Rehearing Order PP 23-24, JA 251-52.

Moreover, the Commission fully explained why the Virginia Parties' interpretation of the regulatory asset accounting standard – as requiring a showing that costs are not recoverable in current retail rates -- misinterprets Commission

policy and is not an accurate statement of the requirements for regulatory asset treatment. Rehearing Order PP 25, 28, 30, JA 252-54. "Regulatory Assets" are defined in the Commission's regulations as: "'specific revenues, expenses, gains, or losses that would have been included in net income determination in one period under the general requirements of the Uniform System of Accounts but for it being probable: A. that such items will be included in a different period(s) for purposes of developing the rates the utility is authorized to charge for its utility services.'" Rehearing Order P 20, JA 250 (quoting 18 C.F.R. Part 101, Definitions (31)). Thus, regulatory asset costs include non-recurring costs that a utility determines are probable of recovery in periods other than the period in which they are incurred. *Id*. P 22, JA 251. Here, the RTO costs at issue were properly treated as regulatory assets because such costs "were an investment in a more efficient transmission system with ongoing benefits to customers." *Id*. P 24, JA 252.

The Virginia Parties rely on the Integration Orders for the proposition that a cost must be shown to be unrecoverable in existing rates for regulatory asset treatment. *See* Br. 33-35; Integration Order P 53; Integration Rehearing PP 40-41. However, when the Commission referred to costs being "unrecoverable in existing rates," Integration Order P 53, this was an expression of the proposition that a cost incurred to benefit future periods that has not been included in determining the utility's currently effective rates, *i.e*. is not recoverable in current rates, should be

amortized over the period in which the benefits are realized. Rehearing Order P 25, JA 252. In other words, the issue is not whether a regulatory prohibition prevented Dominion from recovering its RTO start-up costs; the issue is whether the benefits of these costs accrue to a later accounting period. *Id*. P 28, JA 253.

The Integration Order itself explained that costs incurred prior to customers receiving the commercial benefits of integration into the RTO should be allocated to the period when the related benefits are expected to be realized. Integration Order P 50. This conclusion is based on the matching principle, which assigns costs to the periods in which benefits are expected to be realized. *Id*. P 50 n.50. This rate treatment is *not* based upon the contention that the costs, if not deferred, would be trapped under retail rate caps. *Id*.

As evidenced by the foregoing, therefore, the Commission has consistently applied the matching principle to justify its policy permitting deferral of RTO costs to time periods in which customers enjoy the benefits of RTO participation. Integration Order P 50 n.50; Rehearing Order PP 25, 28, 30, JA 252-254. However, even if the Commission "shift[ed] course" on the standard for regulatory asset accounting treatment, Br. 35, the Commission in any event fully explained its reasons for its holding here. "An agency must be given ample latitude to 'adapt their rules and policies to the demands of changing circumstances.'" *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co*., 463 U.S. 29, 42 (1983) (quoting

Permian Basin Area Rate Cases, 390 U.S. 747, 784 (1968)). An agency may deviate from prior precedent if it provides a reasoned explanation for the deviation. *See, e.g., Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs*., 545 U.S. 967, 1001 (2005) (an agency is free within the limits of reasoned interpretation to change course if it adequately justifies the change); *Baltimore Gas & Elec. Co. v. Heintz*, 760 F.2d 1408, 1418 (4th Cir. 1985) (an agency must provide a reasoned explanation for the failure to follow its own precedents). Thus, even if the Commission's explanation here constituted more than a clarification of policy, the Commission orders should nevertheless be upheld because the Commission provided a reasoned explanation for any change in policy. *Entergy Servs. v. FERC*, 319 F.3d 536, 542 (D.C. Cir. 2003) (Commission did not impermissibly depart from prior precedent where, in the challenged orders, the Commission was clarifying inadvertent statements in prior orders, and even if the orders constituted more than a clarification, the Commission provided a "reasoned explanation for the change in policy").

CONCLUSION

For the reasons stated, the petitions for review should be denied and the Commission's orders affirmed in all respects.

REQUEST FOR ORAL ARGUMENT

Because this case presents significant issues of Commission policy and rate regulation, the Commission respectfully requests that oral argument be held in this case.

Respectfully submitted,

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February 9, 2010

Office of the Attorney General of Virginia, *et al*. v. FERC
4th Cir. Nos. 09-2052, *et al.*

CERTIFICATE OF COMPLIANCE WITH RULE 32(a)

1. This brief complies with the type-volume limitation of Fed. R. App. P 32(a)(7)(B) because this brief contains 11,742 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Fed. R. App. P 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Times New Roman in Microsoft Office Word 2003 14-point and Normal.

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February 9, 2010

ADDENDUM

STATUTES
AND
REGULATIONS

ADDENDUM

PAGE

Statutes:

Federal Power Act

Regulations:

Section 205 of the Federal Power Act, 16 U.S.C. § 824d provides as follows:

(a) Just and reasonable rates
All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful
No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission,
(1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or
(2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules
Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes
Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five-month period
Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f) Review of automatic adjustment clauses and public utility practices; action by Commission; "automatic adjustment clause" defined
(1) Not later than 2 years after November 9, 1978, and not less often than every 4 years thereafter, the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine—
(A) whether or not each such clause effectively provides incentives for efficient use of resources (including economical purchase and use of fuel and electric energy), and
(B) whether any such clause reflects any costs other than costs which are—
(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.
Such review may take place in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.
(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.
(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to—
(A) modify the terms and provisions of any automatic adjustment clause, or
(B) cease any practice in connection with the clause,
if such clause or practice does not result in the economical purchase and use of fuel, electric energy, or other items, the cost of which is included in any rate schedule under an automatic adjustment clause.
(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases (or both) in costs incurred by an electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

Section 313(b) of the Federal Power Act, 16 U.S.C. § 825*l*(b) provides as follows:

(b) Judicial review
Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the United States court of appeals for any circuit wherein the licensee or public utility to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of title 28.

18 C.F.R. Part 101 Definitions (31) provides as follows:

Uniform System of Accounts Prescribed for Public Utilities and Licensees Subject to the Provisions of the Federal Power Act

Definitions

When used in this system of accounts:

31. *Regulatory Assets and Liabilities* are assets and liabilities that result from rate actions of regulatory agencies. Regulatory assets and liabilities arise from specific revenues, expenses, gains, or losses that would have been included in net income determination in one period under the general requirements of the Uniform System of Accounts but for it being probable:

A. that such items will be included in a different period(s) for purposes of developing the rates the utility is authorized to charge for its utility services; or

B. in the case of regulatory liabilities, that refunds to customers, not provided for in other accounts, will be required.

18 C.F.R. Part 101, Account 182.3 provides as follows:

182.3 Other regulatory assets.

A. This account shall include the amounts of regulatory-created assets, not includible in other accounts, resulting from the ratemaking actions of regulatory agencies. (See Definition No. 30.)

B. The amounts included in this account are to be established by those charges which would have been included in net income, or accumulated other comprehensive income, determinations in the current period under the general requirements of the Uniform System of Accounts but for it being probable that such items will be included in a different period(s) for purposes of developing rates that the utility is authorized to charge for its utility services. When specific identification of the particular source of a regulatory asset cannot be made, such as in plant phase-ins, rate moderation plans, or rate levelization plans, account 407.4, regulatory credits, shall be credited. The amounts recorded in this account are generally to be charged, concurrently with the recovery of the amounts in rates, to the same account that would have been charged if included in income when incurred, except all regulatory assets established through the use of account 407.4 shall be charged to account 407.3, regulatory debits, concurrent with the recovery in rates.

C. If rate recovery of all or part of an amount included in this account is disallowed, the disallowed amount shall be charged to Account 426.5, Other Deductions, or Account 435, Extraordinary Deductions, in the year of the disallowance.

D. The records supporting the entries to this account shall be kept so that the utility can furnish full information as to the nature and amount of each regulatory asset included in this account, including justification for inclusion of such amounts in this account.

Virginia State Corporation, et al., v. FERC **Docket No. ER08-1540**
4th Cir. No. 09-2052, *et al*.

CERTIFICATE OF SERVICE

I hereby certify that on February 9, 2010, I electronically filed the foregoing with the Clerk of Court using the CM/ECF System, which will send notice of such filing to the following registered CM/ECF users:

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