UNITED STATES OF AMERICA 152 FERC ¶ 63,025
FEDERAL ENERGY REGULATORY COMMISSION

Potomac-Appalachian Transmission Highline, LLC and PJM Interconnection, L.L.C. Docket Nos. ER09-1256-002 ER12-2708-003

INITIAL DECISION

(Issued September 14, 2015)

APPEARANCES

Kenneth G. Jaffe, Esq., Michael E. Ward, Esq., Ambrea N. Watts, Esq., Morgan E. Parke, Esq., P. Nikhil Rao, Esq., Hector Garcia, Esq., and Amanda R. Conner, Esq., on behalf of Potomac-Appalachian Transmission Highline, LLC.

Pauline Foley, Esq., on behalf of PJM Interconnection, L.L.C.

Paula M. Carmody, Esq., Gary L. Alexander, Esq. and Joseph Cleaver, Esq.; Darryl Lawrence, Esq. and Brandon J. Pierce, Esq.; Meade Browder, Jr., Esq. and Charles Mitchell Burton, Jr., Esq.; Miles H. Mitchell, Esq.; and, Regina A. Iorii, Esq., Robert J. Howatt and John Farber, on behalf of the JCA.[1]

Gary Newell, Esq., and Melissa Alfano, Esq., on behalf of American Municipal Power, Inc.

Sameer Doshi, Esq., on behalf of the Illinois Office of Attorney General.

Harry Ogden, Esq., on behalf of the New Jersey Division of Rate Counsel.

Tad Berger, Esq., on behalf of the Office of Ohio Consumer Counsel.

Darryl Lawrence, Esq., and Brandon Pierce, Esq., on behalf of the Pennsylvania Office of Consumer Advocate.

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[1] For this case, the JCA includes the ad hoc Joint Consumer Advocates group comprising the Maryland Office of People's Counsel, the Pennsylvania Office of Consumer Advocate, the Virginia Office of the Attorney General's Division of Consumer Counsel and the Delaware Division of the Public Advocate; and also includes the Maryland Public Service Commission and the Delaware Public Service Commission.

James Mullins, Esq., on behalf of the Pennsylvania Public Utilities Commission.

Keryn Newman, *Pro Se* and *Alison Haverty*, *Pro Se*, filing briefs.

Mary Ann Allen, *Pro Se*.

Patience Wait, *Pro Se*.

Nicolas A. McTyre, Esq., and Frank X. Kelly, Esq., on behalf of the Trial Staff of the Federal Energy Regulatory Commission.

PHILIP C. BATEN, Presiding Administrative Law Judge.

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I. Decision

1. The Commission set for hearing a series of issues that pertain to the abandonment costs of the Potomac-Appalachian Transmission Highline Project (PATH Project or the Project). The two operating companies that pursued the PATH Project, namely PATH West Virginia Transmission Company, LLC and PATH Allegheny Transmission Company, LLC, are represented in this proceeding by Potomac-Appalachian Transmission Highline, LLC (collectively, the PATH Companies).[2] As indicated below, this Initial Decision resolves the issues for this case.

2. In this case two electric consumers from the state of West Virginia, Karen Newman and Allison Haverty (*Pro Se* Intervenors), challenged the PATH Companies' accounting and placement of certain expenses in accounts that rendered the expenses recoverable from ratepayers. This Initial Decision finds that all of the challenged expenses are not recoverable and must be assigned to unrecoverable accounts.

3. A coalition, under the name of Joint Consumer Advocates (JCA), challenged the PATH Companies' recovery from ratepayers of certain attorney fees under the presumption of prudence standard. On the matter of attorney fees, this Initial Decision has two separate holdings: 1) the PATH Companies may recover from ratepayers those attorney fees for which JCA received the discovery data as requested, and 2) the PATH Companies may not recover from ratepayers those attorney fees for which JCA was denied or did not receive the requested discovery data.

4. The JCA challenged the purchase of certain property for the Kemptown Substation under the presumption of prudence standard. This Initial Decision finds that this purchase was prudent, as well as all of the land purchases that were not challenged in this proceeding. However, this Initial Decision also finds that the losses that the PATH Companies incurred on the past land sales are not recoverable from ratepayers.[3] Further, any future land transactions (whether in the form of transfers to an affiliated entity or sales to third parties) must be accomplished by commercially reasonable procedures if any resulting losses are to be recovered from ratepayers.

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[2] Ex. PTH-1 at 2. The stated purpose of the PATH Companies was to finance, construct, own, operate, and maintain the PATH Project, a joint venture of two utility companies, American Electric Power Company (AEP) and Allegheny Energy, Inc. (Allegheny). *See* PATH Initial Br. at 15-16.

[3] Exhibit PTH-9 lists a summary of the land dispositions at issue in this proceeding. The first 11 properties listed on that exhibit are listed as "sold" and this group of properties comprises the "past land sales" category referenced above.

5. The JCA challenged, pursuant to the presumption of prudence standard, that the PATH Companies should have recommended to PJM Interconnection, L.L.C. (PJM) that the Project be terminated early and that any interim expenses between that point and the actual termination should be denied recovery from ratepayers. This Initial Decision finds that the PATH Companies acted prudently, and therefore the JCA's claim that these interim expenses should not be recoverable from ratepayers is denied.

6. The PATH Companies proposed a 10.4 percent ROE for the abandonment costs that are associated with the PATH project. This Initial Decision finds that a 10.4 percent ROE is unjust and unreasonable and that the just and reasonable ROE is 6.27 percent.

7. The PATH Companies proposed a five year amortization period for the abandonment costs. This Initial Decision finds that this period is just and reasonable.

8. The *Pro Se* Intervenors challenged on equitable grounds that the PATH Companies should be denied the recovery of their attorney fees to prosecute the Formula Rate Challenges in this litigation. This Initial Decision finds that these attorney fees are recoverable from ratepayers.

II. Background and Procedural History

9. At the outset this case presents significant issues of first impression. The Commission's jurisprudence is limited in the area of Order No. 679[4] issues. This case addresses some new issues and gives the Commission a unique one-stop opportunity to review and set policies for the comprehensive litigation scheme arising from Order No. 679. For this reason, all of the attorneys and participants are commended for their assiduous hard work and competence while litigating these issues. They have incalculably enhanced the jurisprudential course of Order No. 679 litigation.

10. The origins of the PATH Project trace back to a May 2005 Commission technical conference at which PJM first presented the transmission project at a conceptual level, but under a different name.[5] In June 2007, the PJM Board identified the PATH Project as a necessary solution to violations of a series of reliability standards, as determined by PJM's 2007 Regional Transmission Expansion Plan (RTEP) Report.[6]

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[4] *Promoting Transmission Investment through Pricing Reform,* Order No. 679, FERC Stats. & Regs. ¶ 31,222 (Order No. 679), *order on reh'g*, Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 (2006), *order on reh'g*, 119 FERC ¶ 61,062 (2007).

[5] *See* Tr. at 2118:15-2122:17; Staff Initial Br. at 4.

[6] Ex. PJM-1 at 12:10-17 (Herling).

11. On February 29, 2008, the Commission issued an order[7] accepting the PATH Companies' formula rate and granting the PATH Companies certain incentives under Order No. 679 for transmission infrastructure investments that would help to ensure the reliability of the bulk power system. Under Order No. 679, utilities are permitted to recover all (100 percent) of their prudently incurred expenses should an eligible project be abandoned for reasons outside of the utility's control.[8]

12. Pursuant to a 2009 settlement and the PJM Open Access Transmission Tariff (OATT), the PATH Companies acquired the obligation to file Annual Updates regarding their rates.[9] The Formula Rate Protocols provide for a process whereby interested persons may review these annual informational filings and challenge any questionable expenses.[10] On January 21, 2011, the *Pro Se* Intervenors filed a formal challenge to the 2010 Annual Update.[11] On December 23, 2011, the *Pro Se* Intervenors filed a formal challenge to the 2011 Annual Update.[12] On September 20, 2012, the Commission set these two formal challenges for settlement and hearing procedures.[13]

13. On September 28, 2012, the PATH Companies made a Federal Power Act (FPA) section 205 filing in Docket No. ER12-2708-000 to recover their prudently incurred abandonment costs from the PATH Project and also to propose a return on equity (ROE) for the abandonment costs. The amount of expenditures that the PATH Companies seek to recover as abandonment costs total approximately $121.5 million, for the period of January 1, 2008, through August 31, 2012.

14. On November 30, 2012, the Commission accepted in part and rejected in part the PATH Companies' section 205 abandonment filing seeking the recovery of approximately $121.5 million. The Commission set the matter for hearing and settlement

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[7] *Potomac-Appalachian Transmission Highline, LLC,* 122 FERC ¶ 61,188, at PP 2, 45 (2008) (February 2008 Order), *order on reh'g and settlement agreement,* 133 FERC ¶ 61,152 (2010) (November 2010 Order).

[8] Order No. 679 at PP 343-344.

[9] *Potomac-Appalachian Transmission Highline, LLC*, 140 FERC ¶ 61,229, at P 1 (2012) (First and Second Formal Challenges Order)

[10] *Id*.

[11] This challenge applies to the 2009 rate year.

[12] This challenge applies to the 2010 rate year.

[13] First and Second Formal Challenges Order at P 79 and ordering para. (C).

judge procedures (Hearing Initiation Order).[14] The Hearing Initiation Order also authorized the Chief Judge to consolidate the PATH Companies' abandonment filing with the *Pro Se* Intervenors' formal challenges docket.[15] On December 13, 2012, the Chief Administrative Law Judge (Chief Judge) consolidated the section 205 abandonment filing with the 2010 and 2011 annual update formal challenges. However, on April 1, 2013, the *Pro Se* Intervenors additionally filed the 2012 Annual Update formal challenge.[16]

15. On June 5, 2013, the Commission issued an order setting the issues in the formal challenges for hearing and settlement judge proceedings and consolidating the formal challenges with the previously consolidated proceedings.[17] On March 24, 2014, the Chief Judge terminated the settlement proceedings and designated the Presiding Judge for the hearing.[18]

16. The hearing commenced on March 24, 2015, and concluded on April 22, 2015. During the hearing, the proceeding participants presented a joint unopposed stipulation in the form of a Staff exhibit that resolved a series of issues, including the PATH Companies' capital structure and the cost of long-term debt to be used to calculate the annual transmission revenue requirement.[19] On June 1, 2015, the Presiding Judge issued an order adopting the Joint Exhibit List. On August 18, 2015, the Presiding Judge issued an order adopting proposed transcript corrections as submitted by the hearing participants. The record in this matter is now closed to any further evidentiary submissions.

17. The two consolidated dockets that comprise this proceeding are Docket No. ER12-2708-003, which concerns the PATH Companies' section 205 filing for recovery of the abandonment costs, and Docket No. ER09-1256-002, which concerns the series of annual

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[14] *PJM Interconnection, LLC,* 141 FERC ¶ 61,177, at P 1 (Hearing Initiation Order).

[15] Hearing Initiation Order at ordering para. (E).

[16] This challenge applies to the 2011 rate year.

[17] *Potomac-Appalachian Transmission Highline, LLC*, 143 FERC ¶ 61,208 (2013) (Third Formal Challenge Order).

[18] Order of Chief Judge Terminating Settlement Judge Procedures, Designating Presiding Administrative Law Judge, and Establishing Track II Procedural Time Standards, Docket Nos. ER09-1256-002 & ER12-2708-003 (March 24, 2014).

[19] Ex. S-26.

update formal challenges involving the accounting and recovery of certain costs through the PATH Companies' formula rate. The JCA was the only party to challenge under the presumption of prudence standard certain expenditures that the PATH Companies sought to recover in their section 205 filing. Among the costs that the JCA challenged as imprudent are approximately $4.8 million for outside counsel legal fees to litigate the certificates of public convenience and necessity (CPCN) proceedings,[20] approximately $29 million for the failure to recommend the timely suspension of the Project,[21] and $6,830,553 million for the purchase of the Kemptown Property.[22] The *Pro Se* Intervenors challenged the PATH Companies' assignment of certain expenses to recoverable accounts and claim that a refund of $6,008,470.70 is owed to ratepayers.[23] The Trial Staff of the Federal Energy Regulatory Commission (Staff) joins the *Pro Se* Intervenors to challenge the accounting of some of these expenses in the recoverable accounts but not all of them. Further, Staff does not challenge the overall prudency of the PATH Companies' expenditures and supports full recovery of other expenditures that are litigated in this proceeding.[24]

III. Annual Formal Challenges (Docket No. ER09-1256-002)

A. Background

18. The *Pro Se* Intervenors initiated formal challenges under the PATH Companies' Formula Rate Protocols to challenge the account assignment of approximately $6,008,470.70[25] that was included in the PATH Companies' recoverable transmission revenue requirements for rate years 2009, 2010, and 2011. These amounts were culled from the published annual updates. The *Pro Se* Intervenors argue that these incurred costs, which were part of the PATH Companies' public education, outreach, and

[20] JCA Initial Br. at 8.

[21] *Id*. at 7.

[22] *Id*. at 62 ("[T]he PATH Companies should be denied recovery of the full purchase price of the Kemptown Property, which was $6,830,553. This should be reflected by reducing the original amortization balance by $6,830,553.").

[23] *Pro Se* Initial Br. at 59.

[24] Staff Initial Br. at 46 ("After reviewing the applicable legal standard and considering the testimony and materials sponsored by PATH and the JCA, Trial Staff supports full recovery of these legal fees and expenses.").

[25] *Pro Se* Initial Br., Attach. 1 (Table of Accounting Reclassifications and Expenditure Removals) .

advertising activities, are not recoverable and should be recorded in non-recoverable accounts because they were intended to influence public officials in support of the PATH Project's licensing process.[26]

19. The sections of the Uniform System of Accounts (USofA) that are at issue in this controversy are Accounts 107, 923, 930.1, and 426.4.[27] Any costs, booked in the first three accounts, are recoverable from ratepayers under the terms of the formula rate. However, under the provisions of the formula rate, no expenditures in Account 426.4 are recoverable.[28] The *Pro Se* Intervenors contend that the funds at issue should have been recorded into Account 426.4, the unrecoverable account. They argue that the intent and purpose of the expenditures were to influence public officials during the Certificate of Public Convenience and Necessity (CPCN) proceedings and the zoning proceedings in the various states where the infrastructure of the Project was sited.

20. During the period from 2009 through 2011, the PATH Companies filed CPCN applications and other actions in three jurisdictions, namely Maryland, Virginia, and West Virginia. To support these applications, the PATH Companies contracted with various public relations firms and other companies to produce advertising, to form public coalitions, and to conduct other advocacy activities that were intended to support the construction of the transmission lines. The *Pro Se* Intervenors argue that these expenditures should have been recorded in Account 426.4 instead of one of the recoverable accounts. The approximate expenditures that are at issue in this case are:

a.	The Reliable Power Coalitions	$1,520,471.03
b.	PATH Education and Awareness Team (PEAT)	$1,411,321.37
c.	R.L. Repass	$148,314.78
d.	Access Point Public Affairs	$75,068.78
e.	Larry Puccio	$93,910.00
f.	General Advertising	$2,618,740.00

[26] *Pro Se* Initial Br. at 3 ("The majority of the expenditures at issue were incurred to build public support and recruit favorable comments to public officials that would, in turn, influence their decisions to approve PATH's state public service commission permit applications.").

[27] *See* 18 C.F.R. pt. 101 (2015).

[28] *See* Ex. S-7 at 12:9-15.

g. Memberships $140,644.74[29]

21. In addition to the *Pro Se* Intervenors' opposition to the accounting treatment of these items, Staff joins the challenge to the accounting only for the Reliable Power Coalitions, Access Point Public Affairs, and the memberships.[30] Staff takes no position on the remaining expenditures.

B. Review of Applicable Law

22. The PATH Companies' Formula Rate Protocols establish the burden of proof in any formal challenge when filed with the Commission. Under the Formula Rate Protocols, the PATH Companies "bear the burden of proving that [they have] reasonably applied the terms of the Formula Rate, including the calculation of the True-up . . . ."[31]

23. The Commission approves the formula rate itself; i.e., the algorithmic sequences that calculate the rates. The Commission does not approve the data inputs or the results from the calculations of the data inputs. Any challenges to the data inputs arise from section 205 or 206 filings or from the formal challenges, as in this case. The Commission has stated:

> [A]ny challenge to the projected costs, True-Up Adjustment, or Material Accounting Change would not require the complainant to bear the ultimate burden of proof. Rather, the Companies will continue to bear the burden of proof, i.e., to demonstrate the justness and reasonableness of the charges resulting from application of the formula rate.[32]

The PATH Companies thus bear the burden to show that they properly assigned all the challenged expenditures to the appropriate accounts. While the *Pro Se* Intervenors collaterally raised questions about the prudence of these expenditures, the legal analysis in this section is limited to addressing whether these expenditures were assigned to the proper accounts, given that the *Pro Se* Intervenors did not submit evidence to challenge the prudence of these expenditures.

24. Two sources of legal authority govern the accounting issues in the formal challenges: 1) the express language of Account 426.4, and 2) relevant Commission

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[29] *Pro Se* Initial Br., Attach. 1 (Table of Accounting Reclassifications and Expenditure Removals).

[30] *See* Staff Initial Br. at 14-31.

[31] Formula Rate Protocols § VII.C.1.

[32] *PJM Interconnection, L.L.C.*, 139 FERC ¶ 61,068, at P 63 (2012).

precedent regarding whether a utility can recover certain expenditures that were spent to influence public officials.

25. The Commission has extensive experience with implementing and adjudicating issues involving Account 426.4. In 1963, the Federal Power Commission (FPC), the predecessor agency to the Commission, issued Order No. 276.[33] The Code of Federal Regulations (CFR) incorporated the order and amended the USofA to include five subaccounts, one of which was Account 426.4, the account at issue here. This account is titled "Expenditures for certain civic, political and related activities," and states in relevant part:

> (a) This account shall include expenditures for the purpose of influencing public opinion with respect to the election or appointment of public officials, referenda, legislation, or ordinances (either with respect to the possible adoption of new referenda, legislation or ordinances or repeal or modification of existing referenda, legislation or ordinances) or approval, modification, or revocation of franchises; or for the purpose of influencing the decisions of public officials . . . .[34]

26. Based on the language of this account, any expenditure by the PATH Companies to influence the decisions of public officials must be included in Account 426.4. Expenses in this account are not recoverable from ratepayers under the terms of the PATH Companies' formula rate. However, in this case the PATH Companies recorded the challenged expenses in other accounts, which would permit recovery. In general, the PATH Companies present the argument that the assignment of these expenditures to recoverable accounts is permitted because the expenditures were related to the PATH Companies' core operations and undertaken to benefit ratepayers.[35] In this regard the PATH Companies chose to include these costs in Accounts 923 and 930.1.

27. Account 923, titled "Outside services employed," states:

> A. This account shall include the fees and expenses of professional consultants and others for general services which are not applicable to a particular operating function or to other accounts. It shall include also the pay and expenses of persons engaged for a special or temporary administrative or general purpose in circumstances where the person so engaged is not considered an employee of the utility.

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[33] 30 F.P.C. 1539 (1963).

[34] 18 C.F.R. pt. 101, Account 426.4.

[35] PATH Initial Br. at 11.

B. This account shall be so maintained as to permit ready summarization according to the nature of service and the person furnishing the same.[36]

28. Account 930.1, titled "General advertising expenses," provides:

A. This account shall include the cost of labor, materials used, and expenses incurred in advertising and related activities, the cost of which by their content and purpose are not provided for elsewhere.

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ITEMS

1. Supervision.

2. Preparing advertising material for newspapers, periodicals, billboards, and other similar items, and preparing or conducting motion pictures, radio and television programs.

3. Preparing booklets, bulletins, and other similar forms of advertisement, used in direct mail advertising.

4. Preparing window and other displays.

5. Clerical and stenographic work.

6. Investigating and employing advertising agencies, selecting media and conducting negotiations in connection with the placement and subject matter of advertising.

Materials and Expenses:

7. Advertising in newspapers, periodicals, billboards, radio, and other similar forms of advertisement.

8. Advertising matter such as posters, bulletins, booklets, and related items.

9. Fees and expenses of advertising agencies and commercial artists.

10. Postage and direct mail advertising.

11. Printing of booklets, dodgers, bulletins, and other related items.

[36] 18. C.F.R. pt. 101, Account 923.

> 12. Supplies and expenses in preparing advertising materials.
>
> 13. Office supplies and expenses.
>
> NOTE A: Properly includible in this account is the cost of advertising activities on a local or national basis of a good will or institutional nature, which is primarily designed to improve the image of the associate utility company or the industry, including advertisements which inform the public concerning matters affecting the associate utility company's operations, such as, the cost of providing service, the associate utility company's efforts to improve the quality of service, the company's efforts to improve and protect the environment, and other similar forms of advertisement. Entries relating to advertising included in this account must contain or refer to supporting documents which identify the specific advertising message. If references are used, copies of the advertising message must be readily available.
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> NOTE B: Exclude from this account and include in account 426.4, Expenditures for certain Civic, Political and Related Activities, expenses for advertising activities that are designed to *solicit public* support or the support of public officials in matters of a political nature.[37]

29. One of the salient cases to interpret whether the costs at issue can be recovered is *ISO New England Inc.*[38] The PATH Companies cite and quote this decision in their initial and reply briefs on numerous occasions, including its language that "the purpose of classifying expenditures in Account No. 426.4 is to highlight them for scrutiny in rate proceedings and require the utility to justify their rate recovery."[39] Despite their focus on the *ISO New England Inc.* decision, this Initial Decision finds that if an expenditure is properly recorded in Account 426.4, then pursuant to the provisions of the PATH formula rate, those expenditures are not recoverable. While *ISO New England Inc.* permitted some recovery under the unique formula provisions and factual circumstances of that case, the formula provisions in the PATH Companies' formula rate make no allowances to recover these expenditures.

30. While the PATH Companies present the argument that the costs at issue were assigned to other accounts because they were related to the PATH Companies' core

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[37] 18 C.F.R. pt. 101, Account 930.1 (emphasis added)

[38] 117 FERC ¶ 61,070 (2006).

[39] *See* PATH Initial Br. at 134 (quoting *ISO New England Inc.*, 118 FERC ¶ 61,105, at P 17 (2007)).

operations and undertaken to benefit its ratepayers,[40] *ISO New England Inc.* further explains that the "intended use" and "reason behind" the expenditure must dictate how the expenditure should be construed for accounting purposes.[41] For example, the Commission has found that "public relations activities involved in a campaign to develop public and legislative support for a utility's *proposal* should be recorded in Account 426.4."[42] The Commission has also noted that timing of certain expenditures is an important consideration regarding whether a cost should be included in Account 426.4, specifically focusing on whether the expense was incurred during a "selection process,"[43] or as in the case of the PATH Project, during its licensing and CPCNs process. This Initial Decision finds no functional difference between the selection process or the CPCN process. In *Alaskan Northwest Natural Gas Transportation Co*. (*Alaskan Northwest*), the Commission discussed a similar accounting question and held:

> The distinction lies in the intended use and reason behind the payments. Expenditures incurred to influence the opinion of the public during the selection process have little or no benefit to the ratepayers, and therefore must be borne by stockholders. Just and reasonable expenditures incurred to keep the general public informed on the progress of the project and other public relations activities are proper expenses to be borne by ratepayers *after operations commence*.[44]

31. The Order No. 679 context of the instant case presents a matter of first impression for the Commission when applying the framework of these legal principles. Most Commission case law addresses utilities that are on-going enterprises providing public service. These utilities, by necessity, must communicate with the public about their operations, improvements, problems, etc. The PATH Companies had no customers and the PATH Project never became operational, yet the PATH Companies felt a significant need to influence public officials to obtain the requisite licensing approvals for the Project. Therefore, to prevail on these accounting matters they must carry their burden to show that their activities were intended to do otherwise.

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[40] PATH Initial Br. at 134-135.

[41] *ISO New England Inc*., 117 FERC ¶ 61,070, at P 42 (2006).

[42] *Id*. P 45 (emphasis added)

[43] *Alaskan Northwest Natural Gas Transportation Co*., 19 FERC ¶ 61,218, at 61,429 (1982) (*Alaskan Northwest*).

[44] *Id.* (emphasis added).

32. The ability of the PATH Companies to show that the subject expenditures 1) addressed core operations, 2) were undertaken to benefit ratepayers, and 3) should be booked elsewhere than Account 426.4 was further compromised because the PATH Companies failed to produce sufficiently detailed evidence. The record evidence in this case contains invoices with cryptic descriptions of the work performed, and lacked other needed documentation such as evidence of the meetings held and the participants involved, and other appropriate documentation to show that the services as performed did not constitute influencing public officials. The burden is on the PATH Companies to make these showings, and the PATH Companies have generally failed to do so in the light of contrary evidence. The record evidence shows that the ultimate aim of the expenditures was to influence the decisions of public officials in an effort to obtain CPCNs and other licensing approvals. Activities of this nature must be recorded in Account 426.4.

33. As a general proposition, the cases that are discussed above suggest that when utilities are seeking selection or CPCN approvals from governmental entities, the utilities should rely on the established governmental approval processes to persuade the officials and not indulge in collateral efforts such as public education, outreach, and advertising activities. If a utility should rely on these collateral activities while pursuing selection or CPCN processes, then it will risk the chance that these costs may not be recovered from ratepayers. If the selection or CPCN application has merit, the governmental selection process provides a sufficient vehicle for the utilities to present their engineering, marketing and economic studies and thereby hope to merit the vote of approval from these officials. In this regard the PATH Companies spent over $8 million on attorney fees to prosecute the CPCNs before the respective governmental bodies, which begs the need for these collateral expenses. Within this analytical framework, the following sections address each of the cost areas that were presented in the formal challenges by the *Pro se* Intervenors.

C. Reliable Power Coalitions

34. The PATH Companies hired contractors, namely Charles Ryan Associates (who in turn hired other contractors) to form three organizations that were collectively called the Reliable Power Coalitions (Coalitions). The Coalitions consisted of West Virginians for Reliable Power, Marylanders for Reliable Power, and Virginians for Reliable Energy. The Coalitions incurred expenses between 2009 and 2011, which amounted to $1,578,618, and recorded them in Account 923, Outside services employed, and in Account 930.1, General advertising expenses.[45] These accounts are recoverable under the provisions of the PATH Companies' formula rates. Based on emails and planning

[45] Ex. S-7 at 7-8.

documents pertaining to the Coalitions that were submitted into the record, the goals of the Coalitions were listed as follows:

> Develop and execute an aggressive and consistent grassroots effort campaign in project area in 11 months
>
> Build base of supporters and create groundswell of support for PATH Project
>
> Create and execute PATH specific messages and responses that cannot currently be delivered.[46]

35. Schedule 1 of the Service Agreement between the PATH Companies and Charles Ryan Associates states that the firm was contracted to develop and implement a strategic plan that:

- Proactively communicates project benefits to key stakeholders, including public officials, community groups, regulators and businesses
- Solicit third party endorsements that would broaden the project's base of support among opinion leaders, elected officials, and other influential stakeholders
- Mitigate opposition by community officials, organizations and affected residents
- Identifies potential allies and stakeholders to serve as ambassadors supporting the project.[47]

36. As the PATH Companies' witness Ruberto stated, "The PATH Companies supported the Reliable Power Coalitions as part of their advocacy for the PATH Project" because the Reliable Power Coalitions "enhanced the prospects that the Project would receive the regulatory approvals it needed."[48]

37. The PATH Companies argue that these expenses are properly recorded in Accounts 923 and 930.1. However, the record contains virtually no descriptive information about the subject activities, aside from the undescriptive invoices in the record. In addition, by the express terms of Account 923, records must be maintained to

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[46] Ex. NH-32 at 1.

[47] Ex. S-2 at 19.

[48] Ex. PTH-51 at 23: 6-7, 10-11.

permit full transparency and identification of the outside services employed: "This account shall be so maintained as to permit ready summarization according to the nature of service and the person furnishing the same."[49] The available documentation of record referring to these services are cryptic at best and show that the services were contracted to influence public officials to favor the Project.

38. The PATH Companies' witnesses explained in testimony that the purpose of the Coalitions was to accomplish these results not by lobbying, but by educating the public.[50] They argued that if a well-informed public supported the Project, then the officials charged with making decisions would be encouraged to likewise support the Project. The members of the Coalitions were recruited to testify before various governmental bodies in support of the Project.[51] The PATH Companies provided all financial support for the Coalitions. The record evidence demonstrates that the Coalitions were not self-recruiting or self-motivating, but were initiated and directed by consultants under the direction of the PATH Companies.[52] While various invoices were presented with dollar figures showing various dates of activity, no descriptive record evidence was provided to demonstrate that the activities were not lobbying as required by Accounts 923 and 930.1.

39. Based on the record, the PATH Companies have not met their burden to show that their assignments of the Coalition expenses were properly placed in recoverable accounts. The expenditures clearly promoted the Project by influencing the decision making of public officials. The PATH Companies' argument that these expenditures should qualify as outside services under Account 923 is misplaced given that this account is generally reserved for the costs of accountants, lawyers, and other professional services to support operations.[53] Therefore, the costs at issue should be recorded in Account 426.4 and not Accounts 923 or 930.1.

40. As stated earlier, the Commission has clarified that the "intended use" and "reason behind" the payment dictates its account assignment.[54] Expenditures that were incurred during the "selection" process, or as the case here, the licensing and CPCN process, "have little or no benefit to the ratepayers, and therefore must be borne by

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[49] 18 C.F.R. pt. 101, Account 923.

[50] Ex. PTH-51 at 24:3.

[51] Ex. PTH-68.

[52] *See generally* Ex. NH-25 at 38, 40, 42, 45, and 46.

[53] Ex. S-7 at 13:12.

[54] *ISO New England Inc*., 117 FERC ¶ 61,070, at P 42 (2006).

stockholders."[55] The stated need, of the PATH Companies to aim their "informational and educational" activities at the governmental approval processes through these Coalitions, speaks to the intent and use of the expenditures as lobbying efforts. As PATH witness Ruberto explained in his answer to why the PATH Companies had engaged in these outreach activities:

> The PATH Project was a massive multi-state undertaking which sought to provide much needed backbone transmission capacity to deliver power from West Virginia to the constrained Baltimore/Washington area. The Project was deemed by PJM to be the most robust and effective solution to criteria violations in central Pennsylvania, the Allegheny Mountain regions and the Baltimore/Washington D.C. area. Given the magnitude and multi-state nature of the Project, the PATH Companies believed it was imperative to engage in public education and outreach activities to assure that information about the PATH Project, the need it would satisfy, and the benefits it would provide was [sic] presented to the public as background for the *state regulatory process*.[56]

41. Based on the record, this Initial Decision assigns all of the expenses for the Coalitions to Account 426.4. The PATH Companies' failure, to provide descriptive invoices or other evidence to describe the exact nature of the Coalitions' work, prevents the PATH Companies from satisfying their burden. Public utilities bear the burden to establish the "validity and accuracy for each of their cost estimates."[57] Perhaps, had the PATH Companies provided clearer records of these activities, a fair argument could have been made that some of the expenses should have been included in recoverable accounts. Record evidence shows that Staff made requests for detailed discovery on information about the Coalitions, their sponsored events, submission of comments, advertising, etc.—but received vague answers at best or no answers.[58] The PATH Companies did not provide any of these necessary details to prove their case.

42. As stated above, Commission precedent clearly establishes that costs, incurred during the "selection process" to influence public officials, are of no benefit to ratepayers. This decision finds no qualitative distinction between the "selection process" and the PATH Companies' CPCN and rezoning pursuits. Here, the PATH Companies' purpose for the activities of the Coalitions was only to attain favorable decisions from

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[55] *Alaskan Northwest* at 61,429.

[56] Ex. PTH-7 at 6-7 (emphasis added).

[57] *Anaheim v. FERC*, 669 F.2d 799, 803 (D.C. Cir. 1981).

[58] *See, e.g.*, Ex. S-8 at 8-9 (PATH Response to Staff's Fourth Set of Data Requests).

public officials on CPCN and other approvals that were required to allow the Project to move forward, and therefore these costs must be recorded in Account 426.4 and are unrecoverable from ratepayers.

D. PATH Educational Awareness Team (PEAT)

43. In addition to the Coalitions above, the PATH Companies spent $1,440,830.10 to fund the activities of the PATH Education & Awareness Team (PEAT) between 2009 and 2011.[59] The PATH Companies recorded the majority of the PEAT expenses in Account 923, Outside services employed. A few of the PEAT invoices were alternatively recorded in Account 930.1, General advertising expenses, and Account 107, Construction work in progress—electric.[60]

44. The PATH Companies and their consultants created PEAT to be comprised of third-party technical experts, environmentalists, and labor and business representatives from West Virginia, Maryland, and Virginia. Some team members performed labor-intensive duties and were paid, while others served as volunteers. The PEAT was formed to educate the public, media, elected officials, and community leaders about the Project, to clear up misconceptions, and to keep those audiences aware of significant milestones concerning the PATH Project.[61] In addition, PEAT created, promoted, and collected signatures on "a petition to support the PATH project." The petition was to be filed with the state commissions.[62]

45. The PATH Companies' plan for PEAT specified the following actions: 1) recruiting speakers for the West Virginia and Virginia public hearings, 2) having local members write letters to the West Virginia Public Service Commission and the Virginia State Corporation Commission, 3) having local workers sign petitions supporting the Project in all three states, and 4) having members write and send letters concerning PATH's National Environmental Policy Act (NEPA) application review.[63] Another list of "labor support" activities included: 1) sending letters to governors, public service commissions, and elected officials (for which the PATH Companies supplied "bullets"

[59] Ex. NH-31.

[60] *See generally* Tr. at 1955:3-7.

[61] Ex. NH-32 at 6.

[62] Ex. NH-37 (PATH petition).

[63] Ex. NH-38 at 6.

and all information for mailing), 2) testifying at hearings, 3) signing petitions, and 4) attending "pro-PATH" rallies around the hearings.[64]

46. The record for the PEAT expenditures suffers from the same infirmities as the Coalitions. The record contains invoices for these expenses, but no descriptive documentation that would assist a fact finder in his effort to discern that their intent and use was anything other than to influence public officials. Therefore, these costs must be recorded in Account 426.4 and are unrecoverable from ratepayers.

E. R. L. Repass

47. The PATH Companies reimbursed their contractor, Charles Ryan Associates, the amount of $331,843.56 for a subcontracted public opinion poll that R.L. Repass (Repass) conducted between 2009 and 2011.[65] The PATH Companies recorded the majority of the Repass expenditures in Account 923, Outside services employed. Three of the Repass invoices were alternatively recorded in Account 107.

48. The PATH Companies take the position that the Repass polling was used to gauge public attitudes toward the PATH Project and to measure changes in public opinion over time.[66] This process, as the PATH Companies argue, helped to determine the degree of effort that was required to educate the public in order to counteract the opposition to the Project and to develop the best targeted outreach and advertising campaigns.[67] As the PATH Companies expert witness Williamson explained in his direct testimony, "in order to educate the public about the need for a project, a utility needs to know the existing state of knowledge and the concerns [that] the public may have."[68] Moreover,

> [i]n order to correct public misperceptions, a utility needs to know what the misperceptions are. Polling and focus groups are important tools to identify areas of concern to members of the public, gaps in their knowledge of issues associated with utility service or transmission project, and areas to which they may be misinformed.[69]

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[64] Ex. NH-38 at 9.

[65] Ex. NH-49.

[66] Ex. PTH-51 at 14.

[67] *Id.*

[68] Ex. PTH-79 at 19:17-18.

[69] *Id.* at 19:18-22.

Williamson also testified that Repass enhanced the prospect for the PATH Project's approval by providing information on the underlying sentiment of the community and data required to craft the PATH Companies' messages to meet local needs.[70]

49. The *Pro Se* Intervenors argue that the Repass surveys and forums were not conducted for educational purposes and did not educate the public, but rather were designed to build public support and acceptance for the PATH Project.[71] In response to this argument, the PATH Companies do not disagree with this characterization, but argue that this conclusion does not prohibit their method of accounting for this expense. The PATH Companies argue that their public education and outreach activities were intended to build support for the Project by providing information about the Project and the reliability needs that the Project would satisfy, and that Repass polling and focus groups helped the PATH Companies to develop messages that were best tailored to achieve this objective. The PATH Companies further argue that those activities were part of the PATH Companies' core operations and provided a direct benefit to ratepayers by helping to craft outreach messaging in order to enhance the PATH Project's base of support.[72]

50. Earlier, this decision established that incantations of "core operations" do not provide sanctuary for these types of expenditures. Based on the record in this case, the *Pro Se* Intervenors make the better argument. The record indicates that the Repass expenditures had the purpose and intent to collect, devise, and disseminate information for one purpose—to have success with the political officials who in the end would have to grant the licensing approvals so that the Project could ultimately be built. All of the activities of Repass, the Coalitions, and PEAT, similarly coalesce around this goal and evidence a concerted effort to influence the decisions of public officials, a characteristic that mandates that the costs of these actions be included in Account 426.4.

51. Additionally, the invoices for Repass expenditures also suffer from inadequate explanation. No records show the methodology of the surveys, the use of the information, and that the information was not merely used to influence public officials. This lack of evidence further demonstrates that the PATH Companies failed to meet their burden of proof.

F. Access Point Public Affairs

52. The PATH Companies contracted Access Point Public Affairs (Access Point) to "represent" them before the Loudoun County, Virginia, Board of Supervisors, and paid

[70] Tr. at 2539:25-2540:9.

[71] Tr. at 2315:18-2316:1.

[72] Tr. at 2548:19-24 (Williamson).

Access Point $115,089.77 between 2009 and 2011.[73] The PATH Companies recorded $75,068.78 of the Access Point expenditures in Account 923, Outside services employed, and included these expenditures in their formula rate annual update and recovered them from ratepayers. Alternatively, the PATH Companies recorded the remainder of the Access Point expenditures in Account 426.4 and did not recover these from ratepayers.[74] As an example of the work performed by Access Point, one of the purchase orders in the record provides in part:

> Access Point will be providing the following services:
>
> - Strategic guidance on next steps in Loudoun County to support opportunities to *influence the Board of Supervisors*
>
> - Continued outreach to key stakeholders and those who *influence* them within Loudoun
>
> - General Assembly member outreach and communications
>
> - Continued message and communications support
>
> - Regular intelligence reporting[75]

53. The PATH Companies take the position that Access Point was engaged to provide information to the public and Loudoun county officials to address a particular transmission line routing issue that could have reduced the impact of the Project on the community and save millions of dollars. Specifically, the PATH Companies argue that Access Point sought to educate the Loudoun County Board of Supervisors about the benefits of the proposed route, which required the modification or release of an easement that prohibited the construction of a transmission line within the easement. Such a result would produce a substantial cost savings and decreased local impact. As part of their duties, Access Point met with county commissioners regarding the release of the easements.

54. The *Pro Se* Intervenors, along with Staff, contend that Access Point's activities were lobbying.[76] But, the PATH Companies argue that neither the *Pro Se* Intervenors nor Staff identifies a single instance in which Access Point made specific requests of the

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[73] Ex. NH-52.

[74] Exs. NH-43 and NH-52.

[75] Ex. NH-53 at 11-12 (emphasis added).

[76] Ex. NH-1 at 61; Ex. S-7 at 16 (Direct Testimony of Craig Deters).

officials with whom it had met. The PATH Companies assert that the evidence shows that Access Point's role was to provide information to the members of the Board of Supervisors and their staff, not to request them to take action.[77] In particular, the PATH Companies contend that Access Point merely explained the ramifications of alternative routing options for the Project. As the PATH Companies' witness Ruberto explained, if the Board of Supervisors would agree to modify the conservation easements, the Project could have used a more direct route through the county, with approximately $20 million in savings to ratepayers and decreased impacts in the local area.[78] The PATH Companies argue that they engaged Access Point to present these options to the county officials and thereby sought to make the PATH Project easier and less costly to construct.

55. The PATH Companies further argue that even though Access Point contacted public officials directly, that fact does not turn the expenditures for these activities into unrecoverable lobbying expenses. For support on this point, they argue that many of the expenses in *ISO New England Inc.* were related to direct contact with public officials and were permitted recovery.[79] They further argue that Access Point activities were directly related to the PATH Companies' existing or proposed core operations and undertaken for the benefit of their ratepayers. As such, they argue that the activities were properly recorded in recoverable accounts.

56. In essence, the PATH Companies argue that Staff and the *Pro Se* Intervenors must prove that Access Point lobbied Loudoun County officials. However, the PATH Companies have the burden of proof on this matter. The purchase order cited above clearly reads as a lobbying contract and uses lobbying-like language. Further, the PATH Companies have presented no detailed invoices which might serve to distinguish Access Point's lobbying activities from non-lobby activities. Without better evidence, the PATH Companies fail to meet their burden. And again, their arguments referring to existing or proposed core operations and the benefits to their ratepayers do not relieve them from presenting evidence to show the nature of the challenged expenditures.[80] And again, the PATH Companies admit that they have limited documentation for these expenses, as evidenced by the following response to a Staff data request: "Access Point made several contacts with Loudoun County Board of Supervisors throughout the project timeline. No records exist on the specific number of contacts made."[81] Additionally, as *Alaskan*

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[77] Tr. at 1618:21-1622:19 (Ruberto).

[78] Ex. PTH-51 at 20.

[79] *ISO New England Inc.*, 117 FERC ¶ 61,070, at P 49 & n.70 (2006).

[80] *Alaskan Northwest; Id*.

[81] Ex. S-2 at 94.

Northwest makes clear, the Commission considers activities undertaken prior to the "selection process, or as here, prior to the issuance of CPCNs, as constituting unrecoverable costs when the expenditures are part of a program to convince state and local officials on the merits of a selection or action.[82]

57. For this reason and the evidence as discussed above, this Initial Decision makes the fair inference that these expenditures were for the purpose to influence public officials, and therefore must be recorded in Account 426.4. This fair inference is further bolstered by the salient fact that the PATH Companies were applying for CPCN and zoning and easement exceptions over which these officials had jurisdiction. The clear implication of any meetings to disseminate information is that the PATH Companies were attempting to influence public officials. The PATH Companies have presented no evidence to dispel this inference, despite the fact that they carry the burden on this issue.

G. Larry Puccio

58. The PATH Companies reimbursed its contractor, Charles Ryan, the amount of $93,910 for the subcontracted services of Larry Puccio, L.C. (Puccio) during 2010 and 2011.[83] Puccio's expenditures were recorded in Account 923, Outside services employed, and these expenditures were included in the PATH Companies' formula rate annual update and recovered from ratepayers.

59. The nature and origins of the PATH Companies' business relationship with Puccio are somewhat amorphous. The evidence shows that the PATH Companies initiated employment discussions with Puccio sometime in December 2009. The discussions continued until around August 2010, when he was paid for the first time.[84] However, the record is unclear if he had done any work by that time. Documents show that his employment by the PATH Companies potentially required a waiver from the West Virginia Ethics Commission of the one year prohibition on lobbying by former state employees:

> Larry told me he has filed a request with the WV [West Virginia] Ethics Commission asking for a waiver from the required one-year prohibition on lobbying by former state employees. He expects the waiver will be granted but

[82] *Alaskan Northwest* at 61,429; *see also Northern Border Pipeline Co.*, 23 FERC ¶ 61,213, at 61,439 (1983).

[83] Ex. NH-55.

[84] *Id*.

> not until January. That means he will not be able to sign a contract to lobby until then. He would not need a waiver to do real estate or R/W [right of way] work.[85]

60. The Consulting Services agreement with Puccio was not signed until June 24, 2010. The agreement provides that he would consult in all aspects of promoting the PATH Project in West Virginia, including government and public relations strategies, but would not provide lobbying services.[86] Internal communications among officials of the PATH Companies show that while the need for Puccio remained in limbo, they continued to discuss ways to make the best use of his services. On July 14, 2010, certain communications indicated that he would be assigned to PEAT,[87] and on October 1, 2010, other communications revealed that the PATH Companies were still unsure about ways to make the best use of Puccio, if at all.[88] By this time, the PATH Companies had paid him over $31,000.[89] From this record review, the evidence suggests that Puccio was paid before his assignments were even formulated.

61. Overall, the PATH Companies paid Puccio $93,910.00. The invoices of record provide little description of his services. When the PATH Companies were asked in discovery to provide additional details, their response was that such records are not available.[90] While the PATH Companies make protestations that Puccio's services were not to lobby and instead were to educate the public and public officials, without proper documentation the only factual inference that can be drawn is that his services were to influence public officials, and the PATH Companies have failed in their burden of proof to show otherwise. This Initial Decision has already found that PEAT served as a vehicle to lobby and to influence public officials. Here, documents show that the PATH Companies planned for Puccio to work in conjunction with the efforts of PEAT. For these additional reasons, the Puccio expenditures must be assigned to Account 426.4.

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[85] Ex. NH-57 at 5.

[86] Ex. PTH-65.

[87] Ex. NH-57 at 39.

[88] Ex. NH-57 at 49.

[89] Ex. NH-55.

[90] *See, e.g.*, Ex. NH-72 at 9 ("RESPONSE: The PATH Companies have conducted a diligent search of their files and have not located any documents responsive to this request other than those provided in response to IND-PATH-II-53.")..

H. General Advertising

62. In 2009 and 2010, the PATH Companies spent $2,618,740 on General Advertising and recorded this amount in Account 930.1, General advertising expenses, and recovered these expenditures from ratepayers. In 2011, the PATH Companies spent $102,560 on general advertising, but did not recover these expenditures from ratepayers. The PATH companies contend that they recorded these latter expenditures in Account 426.4 as a management decision to reduce ratepayer controversy during the annual formula updates, but the expenditures were nonetheless recordable and recoverable in Account 930.1.[91]

63. According to "Note A" of Account 930.1:

> Properly includible in this account is the cost of advertising activities on a local or national basis of a good will or institutional nature, which is primarily designed to improve the image of the associate utility company or the industry, including advertisements which inform the public concerning matters affecting the associate utility company's operations, such as, the cost of providing service, the associate utility company's efforts to improve the quality of service, the company's efforts to improve and protect the environment, and other similar forms of advertisement. Entries relating to advertising included in this account must contain or refer to supporting documents which identify the specific advertising message. If references are used, copies of the advertising message must be readily available.[92]

64. The PATH Companies' arguments on this issue ignore the limitations spelled out above. The PATH Companies argue that advertising is recordable in Account 930.1 under the PATH Companies' Formula Rate to the extent that that the advertising is related to education and outreach.[93] However, the limitation in the description for Account 930.1 contemplates that utilities, which are in operation and benefiting the public, may advertise to promote their good will and to explain their operations and the attending expenses and other operational activities that may affect the standing of the utility in the community. The problem with this case is that the PATH Project was not an operational enterprise and therefore had no good will to promote. The Project was trying to become one and expended funds to promote the licensing and CPCN efforts, which would allow the PATH Companies to become an operational enterprise.

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[91] *See* Ex. PTH-70 at 14-16.

[92] 18 C.F.R. pt. 101, Account 930.1.

[93] Ex. PTH-70 at 5, 14 (Rebuttal Testimony of Cheryl L. Gonder).

65. The PATH Companies' position is further diminished by their failure to produce documentation, despite the regulatory language requiring the retention of records. Account 930.1 requires the retention of documents that *specify the* advertising *message.* The record sorely lacks such documentation. The record shows copies of about 10 brochures[94] and about 25 brochure titles.[95] The record also has vague references to newspaper advertisements and television spots, but nothing informative as to cost or content of the message.[96] On its face, the documentation does not support an expenditure of over $2 million for general advertising as established by the parameters of Account 930.1.

66. Review of the brochures in the record indicates that they are clearly promotional in nature and ultimately intended to influence the action of public officials. They extol the need for reliability and why the project should be built. As *Alaskan Northwest* suggests, the timing of the advertising activities has bearing on the intent and purpose for these expenditures when designating the proper account.[97] With the lack of adequate documentation, the only fair inference to be made on the general advertising expenditures is that they were promulgated to influence public officials and therefore must be recorded in Account 426.4. The PATH Companies have failed to satisfy their burden of proof.

I. Memberships

67. The PATH Companies joined and supported approximately 80 community and professional organizations. As explained by the PATH Companies witness Ruberto, the PATH Companies' memberships in various organizations, including the Maryland Chamber of Commerce, provided the PATH Companies venues in which they could educate business leaders, civic leaders, and the public about the PATH Project. Moreover, these organizations could appreciate and publicize the additional benefits of the Project, such as construction jobs and economic development.[98] In this way the PATH Companies' memberships in various organizations, such as the Maryland Chamber of Commerce, enhanced the prospects that the PATH Project would be licensed. According to witness Ruberto, these efforts were appropriate educational and

[94] *See* Exs. PTH-52, 59, 60, 61, 62, 63, 66, and 69.

[95] *See* Ex. NH-66.

[96] *See generally id*.

[97] *Alaskan Northwest* at 61,429.

[98] Ex. PTH-51 at 25.

outreach activities. As witness Ruberto explained, the business community was a primary focus of the PATH Companies' educational and outreach activities.[99]

68. For all of the reasons which require the other expenditures to be recorded in unrecoverable accounts, those reasons also apply to these membership expenditures, namely that they were to influence public officials during CPCN proceedings for a project that was not operational and not benefiting ratepayers. Additionally, the Commission has already issued clear accounting precedent about expenditures for social and service club dues, and other civic expenditures and subscriptions in various community organizations:

> We believe that expenditures for dues and other payments to community social and service organizations should be classified to the appropriate 426 account, as recommended by our staff. These expenditures are, in general, unrelated to utility operations and proper administration of our Uniform System of Accounts requires that the "below the line" accounting classification of such expenditures be uniformly followed by all public utilities subject to our jurisdiction.[100]

69. The PATH Companies have failed in their burden of proof to show that these expenditures belong in recoverable accounts.

IV. Prudency of Attorney Fees

A. Background

70. From 2009 through 2011, the PATH Companies filed CPCN applications with three jurisdictions, namely Maryland, Virginia, and West Virginia. They hired five outside law firms to prosecute the applications in these jurisdictions. The five law firms were: (1) Watson and Renner (DC); (2) Saul Ewing (MD); (3) Vinson & Elkins (DC); (4) Hunton & Williams (VA); and, (5) Jackson Kelly PLLC (WVA).[101]

71. For the five outside law firms the total amount for legal fees was $4,462,858.75,[102] and the total amount for expenses was $373,329.19,[103] bringing total fees and expenses

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[99] *Id.*

[100] *Pacific Power & Light Co.*, 11 FERC ¶ 61,073, at 61,104 (1980).

[101] Ex. JCA-127 at 1-3.

[102] Ex. JCA-147 (John Toothman's Firm Summary – All Firms).

[103] *Id.*

for the CPCN proceedings to $4,836,187.94. The JCA contends that $2,832,427 of this total constitutes imprudent expenditures and should not be recovered from ratepayers.

72. However, a total of about $8 million dollars altogether was spent by the PATH Companies on legal fees. The JCA expert witness Toothman did not review all the fees because the PATH Companies provided some information too late to be considered in his analysis for the hearing, and some information was not provided at all.[104] These fees amount to an additional $3.9 million in legal fees that were spent on the PATH Project.[105] This figure comprises 1) the fees that FirstEnergy/Allegheny and American Electric Power billed to the PATH Companies for the work of their in-house attorneys, and 2) the fees from outside law firms to litigate the zoning proceedings in Frederick County, Maryland involving the Kemptown Substation.[106]

B. Legal Standard and Analysis

73. As part of their section 205 filing, the PATH Companies seek full recovery of these attorney fees. For utilities that have been granted incentive rates under Order No. 679, the Commission permits 100 percent recovery of all abandonment costs, including attorney fees, should those expenditures satisfy the presumption of prudence standard.[107] Commission precedent requires the intervenor or challenger first to create or establish serious doubt that the challenged expenditures were not prudent and then the burden shifts to the utility to show that its actions were reasonable under the circumstances that prevailed at the time.

74. The presumption of prudence standard derives from the Supreme Court decision *State of Missouri v. Public Service Commission of Missouri*, in which the Court held that a regulatory commission

> is not the financial manager of the corporation, and it is not empowered to substitute its judgment for that of the directors of the corporation; nor can it ignore

[104] See JCA Initial Br. at 128 ("PATH has no documentation of the time that FirstEnergy and AEP in-house attorneys spent on the individual CPCN case.").

[105] *Compare* Ex. PTH-6 (Major Functional Categories of Abandonment Costs) *with* JCA Ex. 147 (John Toothman's Firm Summary – All Firms).

[106] PATH Initial Br. at 104-105.

[107] Order No. 679 at PP 163-167.

> items charged by the utility as operating expenses, unless there is an abuse of discretion in that regard by the corporate officers.[108]

The Commission has explained these principles further:

> [W]e reiterate that managers of a utility have broad discretion in conducting their business affairs and in incurring costs necessary to provide services to their customers. In performing our duty to determine the prudence of specific costs, the appropriate test to be used is whether they are costs which a reasonable utility management (or that of another jurisdictional entity) would have made, in good faith, under the same circumstances, and at the relevant point in time. We note that while in hindsight it may be clear that a management decision was wrong, our task is to review the prudence of the utility's actions and the costs resulting therefrom based on the particular circumstances existing either at the time the challenged costs were actually incurred, or the time the utility became committed to incur those expenses.[109]

75. The Commission has further added that the necessary evidence to establish a serious doubt of prudence requires more than bare allegations[110] and that "[d]irect evidence" is necessary.[111] Establishing a serious doubt regarding prudence requires "reliable, probative, and substantial evidence."[112]

76. With this articulation of the law, the PATH Companies argue that the JCA presented no evidence showing that the PATH Companies were imprudent when they paid the legal fees and expenses in connection with the CPCN applications. The JCA's expert witness acknowledged that he did not apply the prudence standard but instead relied on the ABA's Model Rule of Professional Conduct.[113] He reviewed the billing

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[108] 262 U.S. 276, 289 (1923).

[109] *New England Power Co.,* 31 FERC ¶ 61,047, at 61,084 (1985).

[110] *Iroquois Gas Transmission Sys., L.P.,* 87 FERC ¶ 61,295, at 62,168 (1999).

[111] *Mid-America Pipeline Co., LLC,* 124 FERC ¶ 63,016, at P 976 (2008), *aff'd* 130 FERC ¶ 61,123 (2010).

[112] *Wis. Elec. Power Co.*, 73 FERC ¶ 63,019, at 65,225 (1995), *aff'd in relevant part*, 98 FERC ¶ 61,233 (2002) (citing Section 7(c), Administrative Procedure Act, 5 U.S.C. § 556(d) (2012)).

[113] Ex. JCA-144 at 8:16-12:7.

entries without addressing whether a reasonable utility manager would have paid the bills under the circumstances prevailing at the time.

C. Legal Fees That are Recoverable

77. As stated earlier Tootman did review $4,836,187.94 in legal fees and services. Of this amount, $2,832,427 in legal fees concern billing entries that he flagged as "cryptic" because he had found them ambiguous or lacking in detail. He recommends a 100 percent deduction of cryptic entries, which is a total of $1,141,958.[114] The second largest portion of the legal fees, which witness Toothman questioned, concerns entries for time spent on communications among attorneys in one of the law firms for the preparation of internal memoranda. These fees amount to $1,134,007.[115] He established a fee ceiling to disallow all of these entries.[116]

78. Toothman flagged other entries because they spoke of attendance at a "tech. conference," which Toothman interpreted as a reference to a computer trade show,[117] rather than a technical conference with regulators to address the issues in the CPCN and zoning applications.[118]

79. Toothman disallowed $219,382 of fees for clerical or administrative tasks.[119] Toothman flagged $111,928 in fees for further review that involved travel. Further, Toothman flagged $464,152 which included a disallowance of $268,941 because the CPCN proceedings were not successful.[120]

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[114] This is the total of the amounts shown on the row labeled "Cryptic (QU)" on Exs. JCA-157, JCA-166, JCA-175, JCA-184, and JCA-193.

[115] This is the total of the amounts shown on the row labeled "Internal Communications (IC or IM)" on Exs. JCA-157, JCA-166, JCA-175, JCA-184, JCA-193.

[116] Ex. JCA-144 at 18-19 ("It is normally in the discretion of the tribunal to decide how much to reduce internal communication time. Our calculation of a fee ceiling is based on disallowing all of these entries, in full.").

[117] Tr. at 1549:17-1550:15.

[118] Tr. at 2497:10-25.

[119] Tr. at 1475:1-2; The fee total is the sum of the amounts shown on the row labeled "Clerical or Admin (CL or AO)" on Ex. JCA-157, JCA-166, JCA-175, JCA-184, and JCA-193.

[120] Tr. at 1371:1-7.

80. This Initial Decision finds that these billing entries and the PATH Companies' payment of the bills meet the presumption of prudence standard as set out by the Commission. The record evidence in this case indicates that the law firms submitted the bills to officials of the PATH Companies, and the bills were reviewed and paid.[121] Under the presumption of prudence standard, the JCA witness did not raise serious doubt that the PATH Companies were imprudent when they paid these bills. The JCA witness followed a different standard in his review of the bills. In particular, the JCA witness Toothman referenced as his standard Model Rule of Professional Conduct 1.5(a).[122] This model rule is known as the *Lodestar* method and prohibits excessive legal fees and overhead charges by attorneys. In contrast and as discussed above, the presumption of prudence standard requires a determination as to whether a reasonable utility manager would have paid the bills, in good faith, under the same circumstances, and at the relevant point in time.[123] While the *Lodestar* method does not allow overhead charges to be billed, no Commission rule prohibits such charges.

81. The other category of bills that the JCA raised involved a series of "cryptic" entries. Exhibit JCA-150 contains about 400 pages of billing activities from all five law firms. The exhibit was compiled from the invoices of the law firms. The JCA witness Toothman, with great detail and assiduous effort, examined each entry and made his judgments about them. He gave each entry a code. One of the codes was designated "qu" which represented "cryptic." However, a review of these cryptic entries did not reveal any reason to have serious doubts about their prudence. Looking at them from the perspective of the reviewers at the utility, the entries would have legitimate meaning. For example, some of the "qu" entries are:

a. Meeting with DNR, meeting with client in Annapolis and return.

b. Telephone call with Randy Palmer.

c. Prepare for conference call on "need", participate in conference call.

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[121] Tr. at 2996:22 – 2997:24. While Mr. Rao was not personally involved in the review of the law firms' bills, he based his testimony on conversations "with the individuals who were primarily responsible for the processing of the bills" and his review of emails and other documents. Tr. at 2982:18-24.

[122] *See* Ex. JCA-127 at 4-5 (quoting rule 1.5(a) of the Model Rules of Professional Conduct (2011)).

[123] *New England Power Co.,* 31 FERC ¶ 61,047, at 61,084 (1985).

d. Prepare for conference call; participate in conference call; review revised Joint Defense Agreement; review Hearing Examiner's and PSC decision re Urbana transmission line proposal.

e. Telephone call with R. Palmer, research and draft memo re eminent domain.

f. Finalize Memo re environmental conditions, telephone call with Joe Nelson.

g. Prepare for and participate in conference call.

h. Review preliminary agenda for technology conference; telephone call with R. Palmer and advise via email.

i. Review internal draft for technology conference.

j. Prepare for and participate in conference call re Kemptown Substation.

k. Review conference call agenda; review Linowes memo; teleconference with J. Delaney.

l. Two conference calls re PATH and Kemptown.[124]

82. Applying the presumption of prudence standard to these entries, this Initial Decision finds that these expenses meet the prudence standard as explained above, and they are recoverable from ratepayers.

D. Legal Fees That Cannot be Recovered

83. As stated earlier, the JCA witness Toothman did not receive certain requested data regarding "the fees from outside law firms for representation of the PATH Companies in zoning proceedings in Frederick County, Maryland concerning the Kemptown substation" in time to factor into his analysis for the hearing.[125] He also did not receive any requested data at all for services that were billed by utility in-house counsels.[126] When combined, these fees and services amount to an additional $3.9 million of the total $8.7 million in legal fees and expenses.[127] Of the $3.9 million, only the portion of

[124] Ex. JCA-150 at 1-2.

[125] JCA Initial Br. at 104-105.

[126] Tr. at 1581:5-10.

[127] JCA Initial Br. at 104.

outside legal fees that are assigned to the Kemptown Property is ruled to be recoverable by the PATH Companies. While the JCA's witness Toothman did not receive the Kemptown data in time to incorporate the information into his overall analysis, he nonetheless received the information. The JCA made no petition for additional time before the hearing to permit its witness additional time to incorporate this information into his analysis.

84. However, the portion of the $3.9 million that represents the in-house legal services is held not recoverable by the PATH Companies. The record herein demonstrates that the PATH Companies failed to provide the requested data timely or at all during much of this litigation. The presumption of prudence standard gives the PATH Companies an extraordinary advantage. It allows the PATH Companies to defer presenting evidence on any prudency issues in their case-in-chief, while placing the initial burden on the intervenors to raise serious doubts about the prudency of expenditures. However, this obligation of the intervenors becomes impossible to meet if the PATH Companies do not provide the data when requested. The presumption of prudence standard presupposes that all information about the utility is readily known or obtainable. This Initial Decision holds, therefore, that if the information is not provided or is lost as occurred in this case, then the PATH Companies lose the presumption of prudence and are obligated *ab initio* in its case-in-chief to show by a preponderance of the evidence that its expenditures were prudent. The PATH Companies failed to present any evidence as part of their case-in-chief that "the fees that FirstEnergy/Allegheny and American Electric Power billed to PATH for the work of its in-house attorneys" were in fact prudently incurred. The PATH Companies may rely on the record for this proof; however, the total record lacks any evidence to demonstrate the prudency of these fees.

85. This evidentiary holding presents a matter of first impression for the Commission. This holding should not be misconstrued as imposing a sanction for failure to provide discovery. This holding addresses the burden of proof only. The presumption of prudence allows a utility filing under FPA section 205 to defer presenting its case-in-chief on any prudence issues. However, if the filing utility cannot or does not provide requested data or discovery, information which might constitute evidence of serious doubt, the filing utility cannot "rest on its laurels." Rather, the utility forfeits the protection of the presumption and must proceed with its case-in-chief on the issue. If the filing utility has no evidence, as appears to be the case here, then the utility fails to meet its burden of proof and persuasion. This holding is supported by the Federal Rules of Evidence, which states the general rule of presumptions as follows:

> In a civil case, unless a federal statute or these rules provide otherwise, the party against whom a presumption is directed has the burden of producing evidence to

> rebut the presumption. But this rule does not shift the burden of persuasion, *which remains on the party who had it originally*.[128]

86. As this rule states, despite the presumption of prudence the PATH Companies ultimately must still satisfy the burden of persuasion that their actions were prudent. They cannot meet this burden by withholding or losing evidence that intervenors may require to fashion a case of imprudence. Therefore, this Initial Decision holds that the in-house counsel legal fees and services at issue in this proceeding are unrecoverable by the PATH Companies because they failed to meet their burden of proof in their case-in-chief and burden of persuasion that these expenditures were prudent.

V. Land Transactions

A. Background

87. First, the appalling fact must be stated that the land transactions at issue in this proceeding are the most egregious aspect of the record in this case given that so much land was purchased for the Project and subsequently sold at considerable losses. The PATH Companies purchased 20 individual parcels of real estate for a total cost of $29,873,751.[129] According to the record evidence, the PATH Companies have sold 12 of the 20 properties that they purchased in fee simple.[130] The PATH Companies purchased those 12 properties for a total of $6,615,198[131] and have since sold those 12 properties for a total of $3,004,200.[132] The aggregate loss between the purchase prices and the sale prices is $3,610,998. Additionally, the true amount of the losses is obscured because the selling price for the property at 4420 Lynn Burke Road is listed in one document as sold for $30,000[133] and in another document as sold for $230,000.[134]

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[128] Fed. R. Evid. 301 (emphasis added).

[129] Ex. PTH-9.

[130] Although PTH-9 shows that only eleven properties have been sold to date, JCA Ex. JCA-35 shows that the parcel of real property located at Lot 12, Rivers Edge, Loudon County, VA was sold in October of 2014 for $409,000. This sale is not reflected in PTH-9.

[131] *See* Ex. PTH-9.

[132] *See id.*; Ex. JCA-35.

[133] Ex. PTH-9.

88. The majority of the real property expenses are associated with purchases for the construction of the Kemptown Substation and Welton Spring Substation.[135] The real property associated with the Kemptown Substation is located at "Bartholows Road, Mt. Airy, Frederick County, Maryland" on Exhibit PTH-9.[136] The PATH Companies acquired this 152 acre property for $6,830,553.[137] This property comprises the Kemptown Property that is referenced throughout this Initial Decision.

89. Two other parcels of land were purchased for the Welton Spring Substation.[138] These two parcels are located at "Route 220 Morefield, Hardy County, West Virginia" (Welton Spring Property) on Exhibit PTH-9.[139] In total, the PATH Companies acquired the Welton Spring Property for $14 million.[140]

90. The PATH Companies seek to mitigate the total abandonment cost with the proceeds from any sale or transfer of the real estate.[141] As real property is sold or transferred, the PATH Companies propose that the sale or transfer price be credited against the amortization balance of the abandonment cost going forward,[142] which presumes that the ratepayers will cover the losses. The PATH Companies provide an example of the credit to be applied in Exhibit PTH-22.

91. All of these land purchases and right of way acquisitions were concluded prior to obtaining governmental zoning approvals or the grant of CPCN applications. The PATH

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[134] Ex. JCA-74.

[135] Ex. PTH-9.

[136] *Id*.

[137] *Id*.

[138] *Id*.

[139] *Id*.

[140] *Id*.

[141] Ex. PTH-7 at 14.

[142] Ex. PTH-18 at 10.

Companies' decision makers believed that prudent business judgment required the quick acquisition of these large parcels of contiguous and strategically located lands to accommodate the large proposed substations and associated extra high voltage equipment.[143] Acquiring land in proximity to existing transportation infrastructure that could accommodate the delivery of large, heavy substation equipment, such as power transformers and reactors, was also an important consideration in the purchase of land for construction of the proposed Welton Spring and Kemptown substations.

92. The PATH Companies also argue that similar prudent business judgment required them to purchase properties to permit access to conservation easements and to simplify the routing of the transmission line. These purchases included the River's Edge properties, Dorland Lane, Bear Run, Ashton Woods, and Buck Fever.[144] The PATH Companies also purchased a number of properties that were either in foreclosure or to be auctioned at prices below the costs of easements, which allowed the PATH Companies to improve the planned routing of the transmission line. These purchases included Old Cave Road, Dillons Run Road, and Lot 4 of Blanche Fisher Tract.[145]

B. Prudence of Land Purchases

93. With regard to the land purchases, the JCA focused its prudency challenge on the Kemptown Property and presented the following:

a. At the time that the PATH Companies purchased the Kemptown Property, the Kemptown Property was classified in the "Agricultural" zoning district under the provisions of the Frederick County (Maryland) Code.[146]

b. At the time that the PATH Companies had purchased the Kemptown Property, they knew that the Kemptown Property was classified in the "Agricultural" zoning district under the provisions of the Frederick County (Maryland) Code.[147]

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[143] The purchase price, disposition, sale price, and date of sale for these acquisitions are set forth in Ex. PTH-9.

[144] *See* Tr. at 1686:1-1699:15 (Ruberto).

[145] *See* Tr. at 1699:16-1702:10 (Ruberto).

[146] Ex. JCA-62.

[147] Ex. JCA-63.

c. The PATH Companies admit that at the time they had purchased the Kemptown Property, they knew that they were required to obtain a Special Exception from the Frederick County Board of Appeals in order to construct a substation on the Kemptown Property, unless the Board's local zoning authority was preempted by the Maryland Public Service Commission's (MPSC) issuance of the CPCN.[148]

d. The PATH Companies applied for a Special Exception for the Kemptown Property from the Frederick County Board of Appeals, which was designated Case No. B-10-08.[149]

e. In its "Findings and Decision" issued on December 20, 2010, in Case No. B-10-08, the Frederick County Board of Appeals denied the PATH Companies' application for a Special Exception for the Kemptown Property.[150]

f. The PATH Companies appealed the Frederick County Board of Appeals' decision regarding the Kemptown Property to the Circuit Court for Frederick County, which was docketed as Case No. C-11-0133.[151]

g. On February 21, 2012, in Case No. C-11-0133, Judge G. Edward Dwyer, Jr. of the Circuit Court for Frederick County issued an Opinion in which he affirmed the decision of the Frederick County Board of Appeals in Case No. B-10-08.[152]

94. Based on these representations, the JCA argues that the PATH Companies should be disallowed any recovery from ratepayers pertaining to the Kemptown Property because the expenditure was not prudently acquired. This proposed disallowance amounts to $6,830,553.

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[148] Ex. JCA-65.

[149] Ex. JCA-66.

[150] Ex. JCA-67.

[151] Ex. JCA-68.

[152] Ex. JCA-69.

95. Given that the Kemptown Property and the other land acquisitions were attained to pursue the development of the project under Order No. 679's incentive scheme, these purchases must be analyzed through the prism of the presumption of prudence standard. This analysis requires, as established in earlier sections of this Initial Decision, that the intervenors first show serious doubt as to the prudence of the purchase and that hindsight cannot be a factor in this evaluation.

96. The JCA argues that the Kemptown Property was not zoned for use as a transmission substation when the PATH Companies purchased it, and therefore it should not have been purchased. However, the JCA must show that no "reasonable utility management" would have purchased that property "in good faith, under the same circumstances, and at the relevant point in time."[153]

97. The PATH Companies witness Ruberto explained that the PATH Companies decided to purchase the Kemptown Property at that time because substations "are necessarily one of the very first things that you need when you're doing a transmission project."[154] He also explained the significance of the location of the Kemptown Property for the Project:

> Kemptown is located right at the point where all four 500 kV lines that would enter into Kemptown are located. Any deviation from that spot would necessarily cause additional transmission line extensions to that new location. And typical for a 500 kV transmission line, you're looking at about $5 million a mile.[155]

98. Ruberto also explained that the PATH Companies required a very large, relatively flat piece of property, with good access to transportation for the delivery of large transmission equipment to be installed at the substation.[156] Although the PATH Companies considered other locations for the substations, all were more distant from the connective location of the 500 kV transmission lines and had other undesirable characteristics.[157] The Kemptown Property satisfied all of the requirements for the substation.

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[153] *New England Power Co.*, 31 FERC ¶ 61,047, at 61,084 (1985).

[154] Tr. at 1666:7-20.

[155] Tr. at 1667:6-12.

[156] Tr. at 1667:17-1668:2.

[157] Tr. at 1759:10-1760:23 (Ruberto).

99. Ruberto also testified that the PATH Companies were aware that the zoning of the Kemptown Property did not permit its immediate use as a transmission substation.[158] He explained that the PATH Companies believed that this obstacle could be overcome because:

> We . . . knew that the state had authority over transmission facilities. We believed that if the state saw this as a transmission facility, that they would override local zoning.[159]

100. Ruberto was referring to the authority of the Maryland Public Service Commission (MPSC) to preempt county and local laws, including zoning laws, by issuing a CPCN for a transmission line under its CPCN jurisdiction. The Maryland Court of Appeals (the state's highest court), had ruled decades earlier that the MPSC's authority to grant CPCNs for transmission lines preempted county zoning ordinances.[160] While the MPSC had not previously exercised that authority over transmission substations, as distinct from transmission lines, the PATH Companies expected the MPSC would do so in the case of a substation that, like the Kemptown Substation, was integral to a transmission line project and connected the new transmission line to existing transmission lines, rather than distribution lines serving consumers.[161] As witness Ruberto's testimony explains, the PATH Companies believed that if the MPSC reached the conclusion that the PATH Project was needed to maintain reliability, MPSC would exercise its authority to grant the necessary approvals, including overriding zoning restrictions that would otherwise apply to the Kemptown Property. In a 2009 ruling involving the PATH Companies' application, the MPSC interpreted its preemptive siting authority to extend to "substations that are integral to a proposed transmission line project that requires a CPCN."[162]

101. Based on the record, the JCA has not raised serious doubt that the Kemptown Property purchase was imprudent. As no other issues with the land purchases were raised, this Initial Decision finds that the PATH Companies prudently purchased all of the land in this case, including the Kemptown Property.

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[158] Tr. at 1753:10-17, 1761:8-12.

[159] Tr. at 1761:9-12.

[160] *Howard Cnty. v. Potomac Elec. Power Co.*, 319 Md. 511 (1990).

[161] Tr. at 1761:8-12, 1764:2-6.

[162] Ex. PTH-112 (*In re Application of Potomac Edison Co.*, Order No. 82892, at 8 (Md. Pub. Serv. Comm'n 2009)).

C. Land Dispositions

102. The Commission also set for hearing the issue of the PATH Companies' disposition of the acquired lands and stated that "because the final abandoned cost of real property is unknown at this stage; the inclusion of abandoned cost associated with real property is conditioned on PATH's expeditiously working to dispose of the property at cost or market values, by transfer or sale prior to the end of the five year amortization period."[163] The land dispositions at issue in this case fall into three categories, 1) past land sales, 2) future land transfers, and 3) future land sales.

1. Past Land Sales

103. As stated earlier, the record evidence of the past land sales shows abysmal and inexplicable losses. These losses amount to about half of the aggregate original purchase price of the land. With respect to the land purchases that had occurred prior to the hearing in this case, the applicable standard of proof for the PATH Companies was the presumption of prudence standard, which allows the PATH Companies to defer any proof of prudence in their case-in-chief and puts the initial burden on the intervenors to show evidence of serious doubt that the PATH Companies acted prudently in acquiring the land. However, the land disposition process, which is triggered after a project has been abandoned, is a distinct phase that is separate and apart from the normal operations of a utility and does not fall under the umbrella of the presumption of prudence standard. Rather, reasonableness is the standard of proof to adjudicate the land sales or dispositions, and the burden is on the utility to prove *ab initio* in its case-in-chief the *prima facie* elements to show that it acted in a commercially reasonable manner to sell or transfer the property at the best possible value. The Hearing Initiation Order for this case appears to support this requirement:

> Because PATH has not completed the sale and transfers of land and other assets, we cannot determine based on the record whether self-dealing or cross-subsidization will occur as a result of these future transfers to affiliates, and whether the proposed prices for sales to third parties *are reasonable*. As part of the hearing and settlement proceedings, we therefore direct parties *to consider the reasonableness of such transfers and sales*, including whether future transfers and sales of real property should be reported in periodic reports that identify the parties, date and price of each transaction. Parties in the hearing and settlement proceedings may also consider whether the formula rate should be modified to include such information, which would allow review of the asset sales and transfers under the formula rate annual update process.[164]

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[163] Hearing Initiation Order at P 69.

[164] Hearing Initiation Order at P 68 (internal footnotes omitted) (emphasis added).

104. The clear message in this passage is that if the *future* sales must be reasonable then the past sales must also be shown to be reasonable. The PATH Companies' own FPA section 205 filing also acknowledges that the future dispositions must be reasonable in a section titled "The PATH Companies' Proposal for Closing-out Transactions is Reasonable."[165] Despite the fact that the intervenors did not present any evidence or arguments regarding the past land sales, that does not relieve the PATH Companies of their burden of proof under FPA section 205 to make the prima facie showing that the sales were reasonable. To prevail, a utility filing under section 205 must satisfy all of the elements of its case-in-chief.

105. Failing to present evidence of reasonableness in their case-in-chief, the PATH Companies may rely on the record of the case. A review of the record does not reveal a sufficient showing by a preponderance of the evidence that the past sales were reasonable. The PATH Companies merely presented limited and generalized comments about the process to market the properties and no property-specific evidence. To satisfy the burden that a commercially reasonable sale was accomplished, at the very minimum the record should show with respect to each property:

a. When appraisals were obtained (if any) in relation to when the property was sold;

b. How long the property was on the market before an offer was accepted;

c. The scope of the advertising of the property, whether it was advertised nationally or only locally to limited buyers, a factor especially pertinent to large properties; and,

d. Any considerations that were weighed when deciding to accept various offers, especially offers that were significantly lower than the purchase price.

106. These elements, which are necessary to demonstrate a reasonable commercial effort on the part of the utility to market the property, were not present in the record. Of the 12 properties that were sold, the record shows appraisals for four of the properties.[166] Witness Ruberto testified about the general process to sell the properties, but provided no property-by-property specifics regarding the sales and marketing efforts. Further, his description of the sales process fails to address the important elements as stated above.

[165] PATH September 28, 2012 Section 205 Filing at 12.

[166] Ex. JCA-35.

> PRESIDING JUDGE: Do you have any notion as to what the process would be when a property is sold for an amount almost half of what it was bought for?
>
> THE WITNESS: Well, as far as the process, the properties were—we obtained brokers from the local area, real estate brokers, and they would provide some comparable and help us determine, just like if I was going to sell my own house, help me determine proper prices to list. The properties were listed through those brokers, and ultimately, the market value ended up being the value you could get, which was the market value at the time for the property. And that's really true for all the ones that were sold. It was through that same process.
>
> PRESIDING JUDGE: So is there any special authority that would have to sign off on a deal where the property is sold for half of what it was purchased for?
>
> THE WITNESS: I'm unaware of that.[167]

107. Given the limited evidence in the record, this Initial Decision finds that the PATH Companies did not meet their *prima facie* burden to prove that the marketing process to sell the individual properties at issue was commercially reasonable. For this reason, the PATH Companies cannot recover from ratepayers the losses incurred on the sale of these properties.

2. Future Land Transfers

108. The Hearing Initiation Order for this case expressed concern about the PATH Companies proposal to transfer land to its affiliates, stating "[b]ecause PATH has not completed the sale and transfers of land and other assets, we cannot determine based on the record whether self-dealing or cross-subsidization will occur as a result of these future transfers to affiliates, and whether the proposed prices for sales to third parties *are reasonable*."[168] As part of these proceedings, the Commission

> "*direct[ed]* parties *to consider the reasonableness of such transfers and sales*, including whether future transfers and sales of real property should be reported in periodic reports that identify the parties, date and price of each transaction. Parties in the hearing and settlement proceedings *may* also consider whether the formula rate should be modified to include such information, which would allow review of the asset sales and transfers under the formula rate annual update process.[169]

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[167] Tr. at 1788:18-25, 1789:1-12.

[168] Hearing Initiation Order at P 68 (internal footnotes omitted).

[169] *Id*. (emphasis added).

109. Exhibit PTH-9 lists properties that have yet to be sold (Listed with Realtor) and lists four properties that are designated to be transferred to affiliated companies (To be transferred to affiliate). The combined total purchase price for the properties to be transferred to affiliates is $21,690,553. The first stated property that the PATH Companies plan to transfer is located at "3038 Big Woods Road, Frederick County, MD" (3038 Big Woods Road Property). The 3038 Big Woods Road Property was purchased for $860,000.[170] The current listed owner of the property is PATH Allegheny MD Transmission.[171] The PATH Companies have stated their plan to transfer the 3038 Big Woods Road Property to an affiliated company, FirstEnergy Properties.[172] FirstEnergy Properties is a real estate holding company that is not a public utility with a franchise service obligation.[173]

110. The second stated property that the PATH Companies plan to transfer is located at "Bartholows Road, Mt. Airy, Frederick County, Maryland," otherwise known as the Kemptown Property. The Kemptown Property was purchased for $6,839,553 to construct the Kemptown Substation.[174] The current listed owner of the property is PATH Allegheny MD Transmission.[175] The PATH Companies have stated their plan to transfer the Kemptown Property to an affiliated company, FirstEnergy Properties. Again, FirstEnergy Properties is a real estate holding company that is not a public utility with a franchise service obligation.[176]

111. The third and fourth stated parcels of property that the PATH Companies plan to transfer are located at "Route 220 Morefield, Hardy County, West Virginia," also

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[170] Ex. PTH-9.

[171] *Id*.

[172] Tr. at 1178:21-1179:5.

[173] Tr. at 1178:2-20.

[174] Ex. PTH-9.

[175] *Id*.

[176] Tr. at 1178:2-20.

collectively known as the Welton Spring Properties.[177] The total purchase price for the Welton Spring Properties is listed as $14 million.[178] Both PATH-WV Transmission and PATH Allegheny Transmission currently own interests in the Welton Spring Properties.[179] The PATH Companies have stated their plan to transfer the PATH Allegheny Transmission interest to FirstEnergy Properties.[180] The PATH Companies plan to transfer the PATH-WV Transmission interest to an unidentified AEP real estate property holding company.[181] Both companies are real estate holding companies and neither is a public utility with a franchise service obligation.[182]

112. When expressing its concern about the affiliate transfers in the Hearing Initiation Order, the Commission specifically cited Order No. 707,[183] which "places price restrictions on affiliate transactions for all power and non-power goods and services transactions between franchised public utilities with captive customers and provides that such sales should be made at the higher of cost or market."[184]

113. The PATH Companies argue that Order No. 707 does not control the outcome of the pending affiliate transfers because Order No. 707 only applies to "sales of any non-power goods or services *by a franchised public utility* that has captive customers or that owns or provides transmission service over jurisdictional transmission facilities."[185]

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[177] Tr. at 1175:1-6 (Although not listed as a planned transfer on PTH-9, Mr. Ruberto confirmed at the hearing that the PATH Companies plan to transfer the Welton Spring Properties to an affiliate.).

[178] Ex. PTH-9.

[179] *Id*.

[180] Ex. JCA-212.

[181] *Id*.

[182] Tr. 1178:2-20.

[183] *Cross-Subsidization Restrictions on Affiliate Transactions*, Order No. 707, 73 FR 11,013 (Feb. 29, 2008), FERC Stats. & Regs. ¶ 31,264 (2008) (Order No. 707).

[184] Hearing Initiation Order at n.78.

[185] PATH Reply Br. at 66 (quoting 18 C.F.R. § 35.44(b)(1)(2014) (emphasis

They argue that none of the PATH Companies or their affiliates is a "franchised public utility," which the Commission's regulations define as "a public utility with a franchised service obligation under state law."[186] Therefore, the PATH Companies argue that the "higher of cost or market standard" should not apply to the proposed property transfers at issue in this proceeding.

114. The JCA alternatively argues that the spirit of Order No. 707 should apply and that any transfers to the PATH Companies' affiliates should be at the cost that the PATH Companies paid for the property and not at any lesser market value. The JCA contends that the application of the higher of cost or market standard would ensure that the PATH Companies' ratepayers are treated fairly in these inter-company transactions. The JCA further argues that the PATH Companies' current intent is to transfer the four properties, which were acquired for approximately $21 million, at current market value, and irrespective of cost.[187] The PATH Companies already suspect that the market value will be "less than cost."[188]

115. The PATH Companies' intent to transfer land to their affiliates present a challenging question, as recognized by the Commission in its Hearing Initiation Order.[189] This Initial Decision does not decide whether any future transfers should be subject to Order No. 707's "higher of cost or market" standard.

116. Given the posture of the case and the Commission's position that all dispositions of abandoned property must be reasonable, this Initial Decision holds that if and when the PATH Companies transfer property to an affiliate, those transactions and the proposed recovery of costs must be included in a new section 205 filing. When making this filing, the PATH Companies will have the burden of proof as part of their *prima facie* case to demonstrate that the transfer price to its affiliates was commercially reasonable and at the best possible price as outlined in the above section on Past Land Sales.

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added)).

[186] 18 C.F.R. § 35.43(a)(3).

[187] Tr. at 1179:6-21.

[188] Tr. at 1179:11-13.

[189] Hearing Initiation Order at PP 67-69.

3. Future Land Sales

117. At least four other properties will likely be sold to third parties. As the Hearing Initiation Order directs, these sales must be reasonable. As discussed in the above section on Past Land Sales, merely getting an appraisal and listing the property with an agent is not enough to show a commercially reasonable sale. The PATH Companies must present evidence of their total marketing efforts with *respect to each property*, including but not limited to:

a. When appraisals were obtained (if any) in relation to when the property was sold;

b. How long the property was on the market before an offer was accepted;

c. The scope of the advertising of the property, whether it was advertised nationally or only locally to limited buyers, a factor especially pertinent to large properties; and

d. Any considerations that were weighed when deciding to accept various offers.

118. Again, given the posture of the case and the Commission's position that all dispositions of abandoned property must be reasonable, this Initial Decision holds that if and when the PATH Companies sell these properties, those transactions and the proposed recovery of costs must be included in a new section 205 filing. When making this filing, the PATH Companies will have the burden of proof as part of their *prima facie* case to demonstrate that the selling process was commercially reasonable as outlined in the above section on Past Land Sales.

VI. Imprudence Allegation Regarding the PATH Companies' Failure to Seek Early Termination of the Project

119. The JCA contends that the PATH Companies failed to recommend the suspension of the Project when events were evident that the project should not continue to go forward. The JCA argues that this failure constitutes an imprudent action which should serve to disallow the recovery of certain costs. Specifically, JCA witness Lanzallota testified "I believe that the PATH Companies—as prudent transmission utility companies—should have requested that PJM suspend the PATH Project sometime around the end of 2009 or the beginning of 2010."[190] The JCA also contends that the PATH Companies' recommendation to the Virginia State Corporation Commission (VA-SCC) that they be allowed to proceed with the Project while waiting for the 2010 RTEP

[190] Ex. JCA-109 at 19:20-20:1.

to be completed was not prudent.[191] Based on these allegations of imprudence, the JCA argues that the abandonment costs increased by $29 million, and therefore the JCA advocates that the PATH Companies should be denied recovery of this amount.[192]

120. The presumption of prudence standard governs the adjudication of this issue, which requires the JCA first to raise serious doubt that the PATH Companies did not act reasonably when events required them to recommend suspension of the Project.

121. The evidence shows that the PATH Companies are not authorized to decide and assess questions of whether a regional network transmission project is needed.[193] Unlike the PATH Companies, PJM, as the regional transmission organization (RTO) for the region, in which the Project was planned for construction, is charged with planning and managing the reliability of the transmission network, including the RTEP process.[194] The PATH Companies are not charged to know the full range of information and data on which PJM relies for transmission determinations,[195] and additionally, the PATH Companies had a contractual obligation to construct the transmission projects as assigned to them by PJM.[196] The record supports a finding that the PATH Companies did behave as a prudent utility by proceeding with their assigned obligations until otherwise instructed by PJM. These expenditures are therefore recoverable.

VII. Return on Equity (ROE)

A. Introduction

122. The Commission set for hearing the appropriate return on equity (ROE) that the PATH Companies should receive on their prudently incurred abandoned plant expenses.[197] More specifically, the Commission stated in the Hearing Initiation Order, "[w]e will set all issues raised by the parties for hearing and settlement judge procedures except for the continuation of the 50 basis point ROE adder for RTO participation . . .

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[191] Ex. JCA-109 at 4:10-12.

[192] JCA Initial Br. at 63; Ex. JCA-109 at 4:13-15.

[193] Ex. PTH-46 at 6; Tr. at 912:12-18; PATH Initial Br. at 45-46.

[194] Ex. PTH-46 at 6.

[195] Tr. at 914:13-22.

[196] Ex. PJM-1 at 8-9.

[197] Hearing Initiation Order at P 60.

."[198] Given that the appropriate ROE was clearly an issue that was "raised by the parties" as evidenced by the underlying pleadings and the express language of the Hearing Initiation Order, this issue must be adjudicated here.[199]

123. With regard to the ROE, these proceedings raise an issue of first impression for the Commission. The PATH Companies seek an ROE on abandoned costs for a project that was never used or useful and was never an investment risk, as will be discussed later. The PATH Project was pursued under the electric transmission incentive program of Order No. 679, which provides that should a project be abandoned for reasons outside the utility's control the utility may present a section 205 filing to seek recovery of all of its prudently incurred abandonment costs.[200] While Order No. 679 clearly authorizes the recovery of all prudently incurred abandonment costs, it provides no methodology to set the ROE.

124. However, Order No. 679 does provide some general guidance about setting a rate scheme, and that guidance is instructive for this case. For example, the order states that the reforms are designed to "continue to meet the just and reasonable standard by achieving the proper balance between consumer and investor interests *on the facts of a particular case*" and that it be "applied in a manner that is rationally tailored to the *risks and challenges*."[201]

125. The ROE in this Initial Decision should not be confused with the past ROE that the Commission had ordered and approved for the pre-abandonment stages of the PATH Project, rulings which are not disturbed or overturned by this Initial Decision. Rather, the ROE in this decision only applies prospectively over the period that the PATH Companies will recover their abandoned plant costs.

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[198] *Id*.

[199] *See, e.g.*, JCA, Motion to Intervene, Protest, and Request for Hearing, Docket No. ER12-2708-000, at 13 (filed Oct. 19, 2012); *see also* Hearing Initiation Order at P 18 ("Several parties request that the Commission deny PATH's request for summary disposition and set PATH's formula rates, return on equity, and incentives for full evidentiary hearing.").

[200] Order No. 679 at PP 28, 343-344 ("[T]he Final Rule provides that the Commission will provide assurance of recovery of abandoned plant costs if the project is abandoned for reasons outside the control of the public utility.").

[201] *Id*. P 26 (emphasis added).

B. The Governing Legal Standard

126. On September 28, 2012, the Path Companies made a FPA section 205 filing to recover their prudently-incurred abandonment costs and included in this filing a proposed ROE on the return of those costs.[202] FPA section 205 requires the applicant utility to bear the burden to prove the justness and reasonableness of its proposed rate increases, including the ROE. The overall rate increase as proposed in the FPA section 205 filing at issue here is somewhat unique because it incorporates a request to recover abandonment costs only and seeks an ROE on those costs.

127. While the Commission previously approved a 10.4 percent ROE for the PATH Companies' prior operational status,[203] that rate does not carry over to be the de facto ROE for this instant proceeding, which concerns the abandonment phase. To recover the costs associated with this phase of the Project, the Commission required the PATH Companies to submit a new FPA section 205 filing. As stated *supra*, the PATH Companies' section 205 filing proposed an ROE of 10.4 percent on the abandoned costs. The fact that this requested ROE is the same percentage that was previously approved by the Commission for the PATH Companies' "operational" endeavors is immaterial. The proposed ROE is a new FPA section 205 filing, for which the PATH Companies bear the burden to demonstrate the justness and reasonableness of the their proposed ROE.[204]

128. The PATH Companies' argument that they currently have an ROE of 10.4 percent for this proceeding and that any attempt to reduce the ROE from that percentage must be carried out under the Commission's FPA section 206 authority is not supported by precedent or the procedural posture of this case.[205] The Commission has held that when an applicant files for any rate increase, the applicant bears the burden for each component of the proposed rate "including the unchanged as well as the changed components."[206] The ROE for the abandonment costs currently does not exist, and therefore, any filing to apply an ROE becomes a proposed rate. The PATH Companies' section 205 filing clearly represents a proposed rate increase as they seek to recover abandonment costs

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[202] Hearing Initiation Order at P 8 (2012) ("In its filing…PATH also proposes to change the PATH Companies' existing approved ROE . . . .").

[203] *Id*. P 72 ("Our rejection of the 50 basis point adder pursuant to section 206 of the Federal Power Act results in an ROE of 10.4 percent to become effective as of the date of this order.").

[204] 16 U.S.C. § 824d(e).

[205] See PATH Initial Br. at 90.

[206] *SFPP, L.P.*, 134 FERC ¶ 61,121, at P 46 (2011).

from ratepayers, along with a proposed return on those costs. The PATH Companies agree with this characterization of their filing, stating in their initial brief that "[t]he PATH Companies commenced the proceeding in Docket No. ER12-2708-003 by submitting an application under section 205 of the Federal Power Act *to increase their rates* to recover their abandonment costs."[207]

C. Findings on the Proper ROE

129. This Initial Decision finds that the PATH Companies have the burden of proof to establish the justness and reasonableness of their proposed ROE and must do so as part of their case-in-chief by the preponderance of the evidence standard.[208] Should the Commission agree with the argument of the PATH Companies that the JCA and Staff bear the burden of proof pursuant to section 206 of the FPA,[209] this Initial Decision finds that the record clearly demonstrates that the PATH Companies' proposed ROE is unjust and unreasonable and that the ROE which this Initial Decision establishes, is just and reasonable under a section 206 burden.

130. In instances when the filing utility does not carry its burden to demonstrate that its proposed ROE is just and reasonable, the decisional authority (the Commission itself or the Presiding Judge) may rely on the record evidence to identify and establish the just and reasonable ROE. For example, in *Southern California Edison v. FERC*, the DC Circuit approved the ROE finding of the Commission:

> The Commission was not persuaded by SoCal Edison's arguments [the utility that made the section 205 filing]. Upon consideration of comments submitted at the Paper Hearing, the Commission determined the appropriate proxy group, found that the zone of reasonableness was between 7.80% and 16.19%, and set SoCal Edison's base ROE at the median of that zone, 10.55%.[210]

131. The overall rate of return for a utility is comprised of various components, but the only component at issue in this proceeding is specifically the ROE.[211] Consistent with

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[207] PATH Initial Br. at 89 (emphasis added).

[208] *San Diego Gas & Elec. Co.*, 149 FERC ¶ 61116, at P 45 (Nov. 10, 2014) ("The party bearing the burden of proof will prevail only if the preponderance of evidence supports its position.").

[209] See PATH Reply Br. at 43-44.

[210] *S. California Edison Co. v. FERC*, 717 F.3d 177, 180 (D.C. Cir. 2013).

[211] Hearing Initiation Order at PP 8, 60 (2012); Ex. S-26 (Stipulation Agreement).

Opinion No. 531, the proceeding participants relied on the Commission's two-step discounted cash flow (DCF) methodology to support their respective ROE proposals.[212] The record also comprises ROE analyses and results under the prior one-step DCF methodology should the Commission wish to evaluate record evidence of that approach as well. The one-step DCF methodology and those results are filed in the record should the Commission wish to rely on them instead of the results in this Initial Decision.[213]

132. The proceeding participants proposed differing ROE percentages. The PATH Companies argue for an ROE of 10.4 percent and conducted a two-step DCF analysis to support this figure, stating that this figure "falls within the 8.65% to 10.97% upper end of the ROE zone of reasonableness when applying IBES growth rates."[214] Staff argues for an ROE of 9.13 percent as premised on its own two-step DCF analysis,[215] setting the ROE at the median of its zone of reasonableness. The JCA argues for the ROE to be set at the five year Treasury note rate, which was 1.70 percent on the day before the JCA initial brief was filed,[216] and if not accepted, alternatively advocates for a ROE of 8.57 percent which is at the median of the zone of reasonableness under its two-step DCF analysis.[217]

133. The differences in the proposed ROEs partially derive from the conflicting views about Opinion No. 531's DCF methodology. Another differing factor was the choice of the proxy groups. As for the methodology, Opinion No. 531 establishes that the prevailing capital market conditions must play a role when deciding where the ROE

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[212] *Coakley v. Bangor Hydro-Elec. Co.,* 147 FERC ¶ 61,234 (Opinion No. 531), *order on paper hearing,* 149 FERC ¶ 61,032 (2014) (Opinion No. 531-A), *order on reh'g,* 150 FERC ¶ 61,165 (2015) (Opinion No. 531-B).

[213] Under the one-step DCF methodology, Staff submitted a median ROE of 8.72 percent, JCA submitted a median ROE of 8.52 percent, and the PATH Companies submitted a median ROE of 8.35 percent. *See* Ex. S-14 (Schedule 4), Ex. JCA-142 at 1, Ex. PTH-108A. While Order No. 531 made clear that its two-step DCF holding should apply to pending *complaint* cases, it said nothing about pending section 205 cases such as the instant proceeding. However, this Initial Decision adopts the two-step method for this case, holding is that Order No. 531 applies to both categories. The parties presented no objections on this point. *See* Order No. 531 at n.25 & n.66.

[214] Ex. PTH-97A at 2:14-19, 9:5-11.

[215] Ex. S-16 at 2:20, 5:3.

[216] JCA Initial Br. at 149.

[217] Ex. JCA-138 at 3:8-9.

should be within the zone of reasonableness.[218] Anomalous market conditions would require the ROE to be placed in the upper end of the zone of reasonableness instead of the traditional median location. While the proceeding participants do not dispute this preferred rule, only the PATH Companies believe that economic conditions remain anomalous. The PATH Companies advocate that anomalous market conditions are present, claiming that "[i]nterest rates and other capital market conditions have not fundamentally changed since the Commission found those conditions to warrant an ROE in the upper portion of the zone of reasonableness."[219] Staff and the JCA alternatively argue that the ROE should be set at the median of the zone of reasonableness because they contend that the market is no longer anomalous.[220]

134. The proceeding participants similarly disagree on the role of other elements of the DCF methodology, including the composition of the proxy groups, calculation of dividend yields, and calculation of EPS growth rate forecasts, among others. Despite the litigants' comprehensive and robust presentation of testimony and data to support the merits of their respective DCF methodological applications, this evidence is not dispositive of the ROE question because this Initial Decision finds that none of the proxy groups in the various DCF analyses is appropriate. The risk of these proxies did not correspond to the risks of the PATH Project in this abandonment phase.

135. The Supreme Court decisions in *FPC v. Hope Natural Gas Co.* (*Hope*)[221] and *Bluefield Waterworks & Improvement Co. v. Public Service Commission of West Virginia* (*Bluefield*),[222] the two pillars of modern ratemaking jurisprudence, are regularly relied upon and applied by the Commission,[223] and are instructive on the ROE issue as presented here. The *Bluefield* decision emphasizes that the ROEs must be set according to the "circumstances, locality, and risk" associated with a particular case,[224] while the

[218] Opinion No. 531 at P 41 ("[W]hile the DCF model remains the Commission's preferred approach to determining [sic] allowed rate of return, the Commission may consider the extent to which economic anomalies may have affected the reliability of DCF analyses in determining where to set a public utility's ROE within the range of reasonable returns established by the two-step constant growth DCF methodology.").

[219] PATH Reply Br. at 5.

[220] Staff Initial Br. at 2; Ex. JCA-138 at 2-3.

[221] 320 U.S. 591 (1944).

[222] 262 U.S. 679 (1923).

[223] Opinion No. 531 at PP 15, 17, 39.

[224] *Bluefield* at 693.

Hope decision states "the return to the equity owner should be commensurate with returns on investments in other enterprises having *corresponding risks*."[225]

136. Given *Hope* and *Bluefield's* mandate to evaluate unique circumstances and degree of risk when making ROE determinations, and based on the record evidence, this Initial Decision finds that the PATH Project in its abandonment phase represents very low risk and therefore should receive a correlated ROE despite the PATH Companies' contentions to the contrary.[226]

137. Both Staff and the JCA point to the relative low risk of the abandonment phase. Testimony from Staff witness Keyton articulated this point by stating, "in this particular proceeding, PATH is unique from a *risk perspective* because the PATH Project is abandoned and the purpose of developing an ROE is to determine the reasonable rate that PATH will collect on abandonment costs amortized over a five-year period."[227] Keyton elaborated on this point as follows:

> While an investor should be allowed to collect a return on equity for the equity funds it is providing to PATH, based on a return on equity calculated using risk comparable companies, in this proceeding PATH is unique in that the Commission is allowing it to collect all of its prudently-incurred costs through its formula rate template relating to the abandonment of the Project. Therefore, PATH may be considered less risky than other companies in the proxy group because those companies do not have a guarantee that they will collect all prudently-incurred costs.[228]

138. The record also indicates that at this abandonment phase the PATH Companies have minimal financial risk[229] and minimal operational risk.[230] The JCA witness

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[225] *Hope* at 603 (emphasis added).

[226] *See* PATH Initial Br. at 111-112; Tr. at 769:22-770:5 (Avera).

[227] Ex. S-11 at 60:10-13 (emphasis added).

[228] Ex. S-11 at 60:16-61:1.

[229] *See* Tr. at 3365:8-13 (Keyton) ("A general definition of financial risk is defaulting on their debt. In this proceeding, PATH did not issue any debt. As far as I know, it's a hundred percent equity. So the financial risk to PATH should be minimal based on the definition I just mentioned for financial risk.").

[230] Tr. at 3365:20-21 (Keyton) ("I don't think it would be operating risk since it's no longer in operation.").

Woolridge also testified as to the unique circumstances that are associated with assigning an ROE to the recovery of the PATH Companies' abandonment costs, as evidenced by the following exchange under redirect:

> Q. Can you tell me, are there comparable businesses out there where if the project goes forward, it generated profits and if it fails, the investors still get their money back?
>
> A. In the competitive world, no.[231]

139. Based on the record evidence concerning the low business, financial, and operational risk of the PATH Project in the context of this abandonment phase, this Initial Decision finds that the proxy groups that underlie the ROE calculations in the record do not correspond with the present low risk or lack of risk of the PATH Companies. The proxy groups that all of the witnesses presented were comprised of on-going operational utilities harboring extremely high risks with no opportunity to recoup 100 percent of their losses. The PATH Companies embarked on this project with the full expectation and the right to recoup all of their expenditures that were prudently incurred. The proxy group members that were selected by the witnesses do not correspond in this manner. Proper proxy group selection is the *raison d'etre* when setting ROEs.

140. Considering this finding of the extremely low degree of risk that is associated with the abandonment cost recovery phase of the PATH Project, the establishment of the proper ROE remains the question. The closest risk analysis to the PATH Companies is purchasing five year treasury bonds. The parent utility companies invested and allocated funds to the PATH Companies after receiving the directive from PJM to develop new transmission. Under these circumstances, Order No. 679 guaranteed that they would receive 100 percent of any prudently incurred lost funds should the Project be cancelled. These circumstances put them at the same investment risk as someone who buys government bonds. The holders of these bonds are certain of the return of their money plus interest, or as in this case, a ROE. When the PATH Companies embarked on this undertaking, the Project was under the similar protection or "risk" as bond holders, given that if the Project failed, the PATH Companies would get all their money back. Despite this low risk, the PATH Companies are seeking an inordinate ROE. In this vein, the JCA argues in its initial brief that the PATH Companies' ROE should be set at the rate of a five year U.S. Treasury note, which was at 1.70 percent on the day prior to filing their initial brief in this case.[232] While the JCA's argument has merit, no evidence was presented in the record to support the proposal.

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[231] Tr. at 2828:3-7.

[232] JCA Initial Br. at 149.

141. In this low risk milieu, the PATH Companies have failed to carry their statutory burden to prove the justness and reasonableness of the proposed 10.4 percent ROE in their section 205 filing. Even if the Commission should agree with the PATH Companies that the ROE question falls under section 206 and that the burden of proof is with the Intervonors or third parties, the record evidence of the low risk of the PATH Project in this abandonment phase as outlined above dictates that 10.4 percent is unjust and unreasonable and therefore is rejected. The question now turns to setting a just and reasonable ROE.

142. Order No. 679 states that "our precedents require the establishment of a range of returns and [that] we select an ROE within that range that reflects the facts and circumstances of a particular case."[233] This directive expressly contemplates a two-tier approach: 1) the establishment of a reasonable range of returns or proxies that are based on the corresponding risks, and 2) the selection of an ROE within that range. The quandary here is that the record is devoid of reasonable ROEs that are based on proxies which correspond with the actual low risk of the PATH Project. As stated earlier, all of the witnesses presented varying proxies, and all were on-going and operational utility enterprises. Given that these proxy groups are dissimilar from the PATH Companies' low level of risk at this stage, this decision adopts an ROE of 6.27 percent, which constitutes the JCA's lowest percentage in its range of reasonableness under the two-step DCF methodology.[234] This percentage also represents the lowest ROE that is vetted in the record. The percentage is also more closely align with the actual low risk level of the PATH Companies' abandonment cost recovery given that all of the DCF analyses are inflated due to their reliance on non-corresponding proxy groups that illegitimately heightened the risk profile of the PATH Companies.

143. This finding of 6.27 percent presupposes that the appropriate ROE is much lower, but this Initial Decision is constrained by the limited record evidence and data and declines to fashion a ROE that was not vetted in the record. Should the Commission find that the limitations of the record and the resultant ROE of 6.27 percent is too high, the Commission has the authority itself to devise a more accurate ROE or the authority to order additional procedures to attain a more accurate ROE. While Opinion No. 531 states that the DCF analysis is the "preferred approach" to determine the ROE, the opinion does not state that the DCF methodology is the exclusive approach.[235] Given the unique ratemaking situation presented by Order No. 679's provision for the recovery of all prudently incurred abandonment costs, the Commission may find that the DCF paradigm

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[233] Order No. 679 at P 22.

[234] Ex. JCA-100 at 189.

[235] Opinion No. 531 at P 41.

does not fit the "circumstances, locality, and risk" [236] of the abandonment cost ratemaking here and order a different methodology. Order No. 679 itself states that sometimes risks "are not reflected in a traditional discounted cash flow (DCF) analysis" and therefore another approach may be necessary to honor the Commission's charge to ensure just and reasonable rates.[237]

144. The PATH Companies' arguments to support their proposed ROE are spearheaded by the PATH Companies witness Avera, an expert who is well known to the Commission. He generally argues that the intent of Order No. 679 was to encourage transmission investment. According to Avera, investors who invested in an Order No. 679 project would not have reason to expect that their ROE would be reduced if the project were to be abandoned. Therefore, witness Avera advocates that the 10.4 percent ROE should continue and not be disturbed.[238] The real question is why would investors have no reason to expect a reduction in the ROE should the project be abandoned? Under Order No. 679, an investor can invest in a risky enterprise with the full comfort that he will get all of his money returned if the project fails. Outside of Order No. 679, other enterprises offer no such protections to their investors. Under Order No. 679, while the project is developing, the investor receives a very high ROE as occurred in this case. However, this Initial Decision adopts the better interpretation of Order No. 679 and holds that when the PATH Project was abandoned, the ROE must be reduced in the abandonment phase to reflect the new low level of investment risk. .Such an outcome should not be unreasonable to investors, given that no other economic endeavors present such an extraordinary investment opportunity and protection.

VIII. Amortization Period

145. The PATH Companies propose in their section 205 filing to recover their abandonment costs by using a five year amortization period that spans September 2012 through August 2017.[239] The PATH Companies have the burden to prove that their proposal is just and reasonable. They argue that the evidence in the record is sufficient to meet this burden.[240]

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[236] *Bluefield* at 693.

[237] Order No. 679 at P 27.

[238] *See generally* Tr. at 786-797.

[239] Ex. PTH-18 at 7.

[240] Ex. PTH-18 at 7-11; Ex. PTH-21.

146. However, the JCA did question the PATH Companies' witness Pokrajac during the hearing about the potential for a shorter amortization period, and based on this questioning, the JCA in its initial brief argues for the first time for the adoption of a four year amortization period.[241] The JCA argues that an accelerated amortization period of 48 months would "result in less carrying costs" and thereby save ratepayers money; however, JCA offers no data or documentation from the record to substantiate this specific proposal.[242] In response to the JCA's cross-examination, witness Pokrajac disputed the merits of a shortened and accelerated amortization period, and the record provides no other facts or analysis for an alternative to the PATH Companies' proposed five year period. In addition, the PATH Companies' witness Pokrajac speculated that an accelerated amortization could result in an unreasonable rate impact on customers.[243]

147. Based on the lack of record evidence and facts to support the JCA's position, the PATH Companies' proposed five year period is found to be just and reasonable and is adopted by this Initial Decision.

IX. Recovery of the PATH Companies' Litigation Expenses Associated with the Formal Challenges

148. The *Pro Se* Intervenors make an argument on "equity" grounds: "[i]n the event it is determined that PATH must refund all or part of the amounts in the formal challenged expenditures, equity dictates that PATH should also be ordered to refund the associated litigation expenditures for its failed attempt to justify its actions."[244] The *Pro Se* Intervenors state that ratepayers have been financing the PATH Companies' litigation expenses in this proceeding because "PATH has been recording its challenge-related litigation expenses in operating accounts as they are incurred and collecting them from ratepayers through its formula rate."[245] The *Pro Se* Intervenors do not seek reimbursement of their own litigation expenses, but request that the PATH Companies not be allowed to recover their own litigation expenses from ratepayers.

149. This Initial Decision declines the *Pro Se* Intervenors' equitable request on a number of grounds. First, this issue is beyond the scope of the hearing. The Hearing Initiation Order and the orders on the formal challenges did not set this issue for hearing,

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[241] JCA Initial Br. at 254.

[242] JCA Initial Br. at 254-255.

[243] Tr. at 885:3-5.

[244] *Pro Se* Initial Br. at 39.

[245] *Id*.

and therefore the issue cannot be considered in this proceeding. Second, the request is not consistent with the Commission's longstanding precedent that regulated utilities "are entitled to recover their reasonably incurred rate litigation costs."[246]

150. Further, this Initial Decision is not the final say on the proper treatment of the accounting challenges. The PATH Companies may yet be found to be correct in the various accounting assignments that they have made. In which case, the issue of whether the PATH Companies can recover their litigation expenses on some sort of bad faith basis will be moot. While the Commission may uphold the findings of this Initial Decision on these challenges, such an outcome does not by itself mean that the PATH Companies had no legitimate basis to believe that they could not win, as their position on the accounting issues was not *per se* frivolous when evaluating the issue in the light of the ambiguous precedents which are currently available As stated earlier, the challenged expenditures were spent in a selection or proposal environment, a characteristic that raises a red flag for the Commission. In such an environment the question is whether the expenditures are intended to influence public officials. As litigation in this area becomes more mature, the answer to this question may become more apparent. In such a situation, this equitable argument to deny litigation recovery for bad faith defenses of improper accounting may have merit in future cases.

X. Conclusion

151. The omission from this Initial Decision of any argument or portion of the record that was raised by the parties and participants in their briefs or on the record does not mean that these items were not considered. All facts and arguments were given due consideration.

[246] *SFPP, L.P.*, 137 FERC ¶ 61,220, at P 39 (2011).

Order

152. It is ORDERED that this Initial Decision shall be of full force and effect in accordance the "finality" provision in Rule 708(d) of the Commission's Rules of Practice and Procedure.[247] Pursuant to Rule 711, any participant in this proceeding may file a brief on exceptions to this Initial Decision no later than 30 days after its issuance.[248]

Philip C. Baten
Presiding Administrative Law Judge

[247] 18 C.F.R. § 385.708(d).

[248] 18 C.F.R. § 385.711(a).

Document Content(s)