119 FERC ¶ 61,238
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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

Commonwealth Edison Company and Commonwealth Edison Company of Indiana, Inc.	Docket Nos. EL07-41-000, ER07-583-000, and ER07-583-001

ORDER DENYING PETITION FOR DECLARATORY,
ACCEPTING IN PART, AND REJECTING IN PART,
PROPOSED FORMULA RATES, SUBJECT TO CONDITIONS AND
ESTABLISHING HEARING AND SETTLEMENT JUDGE PROCEDURES

(Issued June 5, 2007)

1. On March 1, 2007, Commonwealth Edison Company, on behalf of itself and its wholly-owned subsidiary, Commonwealth Edison Company of Indiana, Inc. (collectively, ComEd), filed a petition for declaratory order (petition) in Docket No. EL07-41-000, requesting that the Commission approve its proposed incentive rate treatments for two transmission projects in Chicago, Illinois, as consistent with Order No. 679.[1] ComEd seeks a declaratory order approving an incentive rate of return (ROE) rate treatment amounting to a 150 basis point adder for the two specified projects, as well as

[1] *Promoting Transmission Investment through Pricing Reform*, Order No. 679, 71 Fed. Reg. 43,294 (July 31, 2006), FERC Stats. & Regs. ¶ 31,222 (Order No. 679), *order on reh'g*, Order No. 679-A, 72 Fed. Reg. 1,152 (January 10, 2007), FERC Stats. & Regs. ¶ 31,236 (2006) (Order No. 679-A), *order on reh'g*, 119 FERC ¶ 61,062 (2007).

the ability to recover 50 percent construction work-in-progress (CWIP) in rate base for Phase II of the West Loop Project.[2]

2. In a companion filing, submitted pursuant to section 205 of the Federal Power Act (FPA)[3] (section 205 filing) in Docket No. ER07-583-000, ComEd seeks to implement a cost-of-service formula rate to recover its revenue requirement for all transmission facilities turned over to the operational control of PJM Interconnection, L.L.C. (PJM). ComEd states that no incentive rate treatments or associated revenues are included in the section 205 filing. Instead, ComEd claims that the proposed formula rate is designed to accommodate inputs reflecting incentive rate treatment upon approval of such treatment by the Commission and an additional section 205 filing is therefore unnecessary.

3. ComEd states that the Commission has previously encouraged transmission owners within PJM to file formula rates, and it argues that its formula is fundamentally similar to a cost of service formula recently approved by the Commission.[4] ComEd also states that its formula rate includes a base-level ROE request of 11.7 percent, which is the midpoint of the zone of reasonable returns that range from 7.8 percent to 15.6 percent.[5] ComEd seeks a 50 basis point incentive ROE adder to reward its continued participation in the PJM regional transmission organization (RTO), which increases the overall

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[2] As described below, the West Loop Project is one of the two specified projects, and ComEd has broken the West Loop Project into two phases. Phase I was placed into service in December 2006, and Phase II is scheduled to be put into service by June 1, 2008.

[3] 16 U.S.C. § 824d (2000).

[4] *See Baltimore Gas & Elec. Co. and PHI Cos.*, 115 FERC ¶ 61,066 (2006) (*Baltimore Gas & Elec.*).

[5] ComEd states that the zone of reasonableness is based on a discounted cash flow (DCF) analysis using a 15 company proxy group. *See* ComEd section 205 filing, Appendix D, Exhibit No. CWE-201 at 1. The proxy group consists of: American Electric Power Corp., Consolidated Edison, Inc, Constellation Energy Group, Dominion Resources, Inc., DPL, Inc., Energy East Corp., Exelon Corp., FirstEnergy Corp., FPL Group, Inc., Northeast Utilities, NSTAR, Pepco Holdings, Inc., PPL Corp., Public Service Enterprise Group, Inc., and UIL Holdings Corporation.

allowed ROE to 12.2 percent. ComEd also seeks the ability to include 50 percent CWIP in rate base for *all* transmission investment *indefinitely*, pursuant to Order No. 298.[6]

4. On March 30, 2007, the Commission issued a deficiency request, directing ComEd to submit additional support for both its incentive requests in the petition and its section 205 filing. On April 12, 2007, ComEd filed a response to the deficiency request (deficiency response), renewing its request for an effective date of May 1, 2007.

5. For the reasons discussed below, we will deny ComEd's petition for a declaratory order. We will also accept ComEd's proposed formula rate, subject to a nominal suspension and conditions, to become effective May 1, 2007, as requested, subject to refund. In addition, we will establish hearing and settlement judge procedures.

I. Background

A. ComEd's Proposed Incentive Rate Treatment

1. Description of the Projects and the Proposed Incentives

6. ComEd requests incentive rate treatment for two projects (Projects). The first project is the West Loop Project, a new high voltage transmission upgrade project that is part of a major expansion of ComEd's transmission network in Chicago. ComEd estimates that the entire West Loop project will cost approximately $345 million.[7] ComEd has broken the West Loop Project into two phases. Phase I, a 138 kV switchyard, was placed into service in December 2006. Phase II of the West Loop

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[6] *See Construction Work In Progress for Public Utilities; Inclusion of Costs in Rate Base*, Order No. 298, 48 Fed. Reg. 24,323 (June 1, 1983), FERC Stats. & Regs. ¶ 30,455, *order on reh'g*, Order No. 298-A, 48 Fed. Reg. 46,012 (Oct. 11, 1983), FERC Stats. & Regs., ¶ 30,500 (1983), *order on reh'g*, Order No. 298-B, 48 Fed. Reg. 55,281 (Dec. 12, 1983), FERC Stats. & Regs. ¶ 30,524 (1983) (Order No. 298). ComEd's request in the petition for approval to include 50 percent of CWIP in rate base for Phase II of the West Loop project is in addition to this request here for approval to include 50 percent CWIP in rate base for *all* transmission investment. Therefore, ComEd is effectively requesting approval to include 100 percent of CWIP in rate base for Phase II of the West Loop project.

[7] Approximately $95 million of Phase I of the West Loop Project costs were closed to plant in service in December 2006, leaving $250 million remaining, according to ComEd's petition at 21.

Project, which involves construction of a 345 kV switchyard, two new 345 kV lines, and two 138 kV lines, is scheduled to be put into service by June 1, 2008.

7. The second project is the Grenshaw Project, which was placed into service in May 2006, at a cost of $48 million.[8] The Grenshaw Project consisted of the construction of a 138 kV switchyard, the reconfiguration of two 138 kV transmission lines, and the reconfiguration of two 138 kV distribution lines.

8. ComEd proposes to use cross-linked polyethylene cable (XLPE cable) for both Projects as an underground transmission cable, one of the "advanced transmission technologies" as defined by section 1223 of the Energy Policy Act of 2005 (EPAct 2005).[9] ComEd states that the XLPE cable will have lower operating and maintenance costs and will generally have a higher capacity than more conventional technologies. ComEd states that the XLPE cable will also reduce operational risk and exposure to environmental hazards from oil spills.[10]

9. ComEd requests the following incentive rate treatments for the West Loop and Grenshaw Projects: (1) a 150 basis points ROE incentive rate adder above the base ROE (not to exceed the upper end of the zone of reasonableness), that will be determined pursuant to the proposed formula rate in Docket No. ER07-583-000, to be applied to: (a) the net transmission plant-in-service for the completed Grenshaw Project, (b) the net transmission plant-in-service for the completed Phase I of the West Loop Project, (c) the CWIP balance for Phase II of the West Loop Project, and ultimately, (d) the net transmission plant for Phase II of the West Loop Project,[11] and (2) the ability to include in rate base the additional 50 percent of CWIP associated with Phase II of the West Loop Project.

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[8] ComEd petition at 9.

[9] Pub. L. No. 109-58, §1223, 119 Stat. 594, 961-62 (2005).

[10] ComEd petition, Attachment B at P 16.

[11] ComEd does not ask for a specific ROE to be established in the petition but rather asks that the specific ROE be determined through the accompanying section 205 filing. ComEd petition at 4, n.8.

2. Eligibility for Incentive Rate Treatment

10. ComEd states that the West Loop Project received Certificates of Public Convenience and Necessity from the Illinois Commerce Commission (Illinois Commission), authorizing the project's construction, operation, and maintenance. Further, the West Loop Project was approved in the PJM Regional Transmission Expansion Planning (RTEP) process as two "baseline upgrade projects."[12] ComEd argues that the West Loop Project qualifies for incentive rate treatment under Order No. 679 because it satisfies the two following rebuttable presumptions: (1) the project has received construction approval from an appropriate state commission or siting authority, provided that these approval processes require that a project ensures reliability or reduces the cost of delivered power by reducing congestion, and (2) the project results from a fair and open regional planning process that considers and evaluates projects for reliability and/or congestion and is found acceptable to the Commission. ComEd contends that both approval processes require that the proposed transmission lines ensure reliability and notes that the Commission has previously approved the PJM RTEP for identifying expansions necessary to support reliability and competition.

11. ComEd states that no certificates were required from the Illinois Commission for construction of the Grenshaw Project[13] and that the Grenshaw Project was accepted in the PJM RTEP as a transmission owner-initiated (TOI) project.[14] ComEd acknowledges that PJM has not determined that the Grenshaw Project is required in order to meet reliability criteria, thus not qualifying for the rebuttable presumption. Nonetheless, ComEd argues that the Commission should find that the Grenshaw Project is eligible for incentives because it would improve reliability. Specifically, ComEd states that it has a binding

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[12] Listed as projects b0236.1 and b0236.2 under the PJM RTEP. Baseline upgrades are defined by PJM as "those that directly benefit one or more transmission owner zones for the purposes of maintaining reliability, typically for load growth" and include "economic upgrades – transmission upgrades needed to mitigate unhedgeable congestion." ComEd petition at 7.

[13] ComEd explains that it had a binding commitment with the City of Chicago to construct the Grenshaw Project, as part of a comprehensive discussion with the City on reliability and franchise issues. ComEd deficiency response at 8.

[14] Listed as project TOI275. TOI upgrades are those projects proposed by transmission owners to satisfy local reliability requirements. ComEd petition, Attachment B at P 23.

commitment with the City of Chicago to construct the Grenshaw facilities,[15] as the project is part of a major program to convert the network from a "hub and spoke" design to a more reliable network design.[16] ComEd acknowledges that this project provides a higher level of reliability standards than required by North American Electric Reliability Corporation (NERC) Reliability Standards, ReliabilityFirst Corporation (ReliabilityFirst) Planning Standards, and PJM RTEP or ComEd criteria, and it states that the Commission has recognized that more stringent reliability standards may be appropriate to address the needs of major cities.[17]

12. Although ComEd recognizes that the Commission has clarified in Order No. 679-A that incentive rate treatments would not apply to historical transmission investment, it maintains that the fact that construction of the Grenshaw Project and Phase I of the West Loop Project have been completed should not impact their eligibility for incentives. ComEd notes that the Projects have been, or will be, placed into service after August 8, 2005, the specified effective date of Order No. 679.[18] Further, ComEd argues that it is not seeking incentives for its historical transmission investment as none of the costs incurred by ComEd for the West Loop and Grenshaw Projects have been previously included in rate base or otherwise recovered in rates. ComEd also suggests that to deny incentives on this recently-constructed transmission infrastructure may send the wrong signal to investors contemplating investment in transmission infrastructure.

3. ComEd's Nexus Showing

13. ComEd argues that its proposed incentives have a nexus, or are rationally related, to the West Loop and Grenshaw Projects for several reasons.

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[15] ComEd deficiency response at 8.

[16] ComEd petition, Attachment B at P 22. Specifically, the Grenshaw project is intended to create redundancies in the Chicago central business district, so that in the event of the loss of the Taylor Substation, the impact to the Chicago central business district would be mitigated.

[17] ComEd petition at 6 (*citing Policy Statement on Matters Related to Bulk Power System Reliability*, 108 FERC ¶ 61,288 at P 3 (2004)).

[18] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 34. ComEd notes that while the Projects were not placed into service prior to August 8, 2005, some costs associated with the Projects were incurred *prior to* August 8, 2005, and ComEd has included these costs in its request. ComEd petition at 6.

14. ComEd contends that the Projects are not routine transmission investments but rather represent the most expensive and complex transmission infrastructure investment ever made by ComEd.[19] ComEd states that the cost associated with both Projects is roughly equivalent to the entire cost incurred for all transmission plant additions over the four-year period from 2001-2004.[20] ComEd submits that completion of the West Loop Project entails significant risks associated with obtaining the necessary easements to run underground transmission cables and two tunnels beneath the Chicago River, as well as technological risks associated with constructing underground cables and tunnels beneath the Chicago River. ComEd also argues that the West Loop Project is a multi-year project that will significantly improve reliability in Chicago, and ComEd is entitled to the requested incentive ROE for both Projects in recognition of its commitment to provide reliable service, over and above the minimum required by NERC Reliability Standards, to critical load in the Chicago central business district.

15. Finally, ComEd asserts that the incentives it seeks are necessary to provide adequate revenues to finance the Phase II of the West Loop Project and to maintain ComEd's credit quality. ComEd argues that the additional cash flow provided by the inclusion of 100 percent of CWIP in rate base (*i.e.*, the requested 50 percent CWIP in rate base in the petition plus the requested 50 percent CWIP in rate base for all new transmission proposed in the section 205 filing) and the incentive ROE will reduce the amount of borrowing required to complete Phase II of the West Loop Project and will have a favorable impact on credit metrics, thereby enhancing ComEd's credit quality. ComEd states that both ComEd and its customers benefit from an enhanced credit quality because this will tend to reduce its future cost of capital.

16. ComEd states that the turbulent conditions in the energy industry generally lead analysts and bond rating agencies to focus on measures of cash flow as key indicators. ComEd states that, as a result, the greater risk associated with higher levels of non-cash earnings—such as Allowance for Funds Used During Construction—would ultimately be reflected in higher rates of return required by investors. ComEd argues that investors recognize that including CWIP in rate base is an important tool that supports a utility's financial integrity and attenuates some of the financial risks associated with new infrastructure investment. ComEd notes that its corporate credit rating already occupies the lowest rung on the investment grade ladder at BBB.[21]

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[19] ComEd petition at 12.

[20] ComEd petition, Attachment A at P 5.

[21] ComEd petition, Attachment C at P 36-38.

17. In recognition of Order No. 679-A's requirement that an incentives applicant consider the effect that certain incentives may have on risk and whether an incentive ROE is appropriate when combined with incentives that lower risk, ComEd argues that recovery of the additional 50 percent of CWIP in rate base for Phase II of the West Loop Project will only change the timing of cost recovery, not the absolute amount. Therefore, ComEd contends that the CWIP incentive will not have a measurable impact on investors' overall risk perceptions of the company, and thus there is no basis to reduce the requested ROE incentive adder.[22]

18. ComEd argues that the requested incentives have a relatively small impact on ComEd's revenue requirement, stating that the requested 150 basis point adder will result in a revenue increase of $5.1 million per year. ComEd states that the requested additional 50 percent CWIP in rate base for the West Loop Phase II will result in $10.6 million a year revenue increase. When asked to explain why the ROE incentive is tied to completed projects, i.e., how the requested return on equity is sufficient to *attract new investment* per Order No. 679, ComEd provided the following in its response to the deficiency letter: (1) these projects are placed into service after the effective date of Order No. 679;[23] (2) ComEd is entitled to the requested return on equity for both projects in recognition of the commitment to provide reliable service, over and above the minimum required by NERC Reliability Standards, to critical load in the Chicago central business district;[24] and (3) denying incentive rate treatment on these completed projects "would generally send the wrong signal to investors contemplating a decision to commit capital to an expanded transmission grid."[25]

B. <u>Proposed Formula Rate</u>

19. On March 1, 2007, ComEd submitted revised tariff sheets for the ComEd pricing zone under Attachment H-13, Schedule 7 and Schedule 8 of the PJM Open Access Transmission Tariff (OATT),[26] to reflect a formula cost of service for its Network

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[22] ComEd petition, Attachment C at P 47.

[23] ComEd deficiency response at 4.

[24] *Id.* at 5-6.

[25] ComEd petition, Attachment C at P 28.

[26] The proposed tariff sheets are designated under PJM's FERC Electric Tariff Sixth Rev. Vol. No. 1, as Sixth Rev. Sheet No. 245, Seventh Rev. Sheet No. 245A, Twelfth Rev. Sheet No. 247, Fourth Rev. Sheet No. 247.01, Fifth Rev. Sheet No. 314A,

(continued)

Integration Transmission Service, Long Term Firm and Short Term Firm Point-to-Point Transmission Service and its Non-Firm Point-to-Point Transmission Service.

20. ComEd states that the formula rate is designed to track increases and decreases in actual costs and projected capital additions. ComEd states that there is a true-up mechanism that will be implemented following the end of a rate period to ensure that any deviation from actual costs is reflected in an adjustment (with interest)[27] to the annual transmission revenue requirement in the subsequent rate period.[28] ComEd's proposed "rate year" extends from June 1 of the current year to May 31 of the following year. ComEd states that true-ups and charges will be posted on the PJM website on or before May 15 of the following year, when the Form 1 for the "rate year" becomes available. ComEd affirms that it will make an informational filing at FERC to reflect the updated data, consistent with the Commission's order in *Duquesne Light Co.*[29]

21. ComEd proposes that the initial rate year be a 13 month period, and every year thereafter, a 12 month period, ending May 31 of each year. ComEd states that PJM will use ComEd's Net Annual Transmission Revenue Requirement produced by the formula rate, together with the prior year's coincident-peak load, to calculate charges for ComEd's Long Term Firm and Short Term Firm Point-to-Point Transmission Service and its Non-Firm Point-to-Point Transmission Service under Schedules 7 and 8 of the PJM OATT, respectively.

22. ComEd notes that while it is requesting incentive ratemaking treatment for two transmission Projects in a separate but contemporaneous filing, none of the incentive ratemaking treatments or revenue associated with these incentive treatments are incorporated in ComEd's formula rate filing.[30] ComEd notes that once the Commission approves the incentive ratemaking treatments, the formula rate proposed herein is preset

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Second Rev. Sheet No. 314A..01, and Original Sheet Nos. 314A.02 through Original Sheet No. 314A.27.

[27] In accordance with 18 C.F.R. § 35.19a (2007).

[28] The true-up mechanism is contained in Attachment 6 of the formula rate, Original Sheet No. 314A.18.

[29] 118 FERC ¶ 61,087 at P 66 (2007), *reh'g pending* (*Duquesne*).

[30] With the exception of the 50 basis point ROE adder for ComEd's participation in an RTO, *i.e.*, PJM.

to accommodate any incentive rates. ComEd states that the formula rate is modeled after formula rates previously accepted by the Commission,[31] with the following exceptions:

- *CWIP*: the request for inclusion of 50 percent Construction Work in Progress (CWIP) in rate base for the purposes of earning a return on CWIP.
- *Account 219*: the removal of the effect of accumulated other comprehensive income (FERC Electric Account No. 219) from the calculation of the total value of common stock in line 121 of the formula rate.
- *Distribution Facilities*: the inclusion of costs incurred by ComEd to utilize the lower voltage transmission system of Commonwealth Edison Company of Indiana, Inc., which is integrated with the ComEd system and is under the functional control of PJM. (Booked to Account 565)
- *Direct Assignment Costs:* the direct assignment of costs, including associated depreciation reserve and depreciation expense, related to communications equipment (for example, SCADA equipment used to monitor the transmission and distribution system). The allocation is based upon a location-by-location study of the equipment and has been approved in ComEd's two previous transmission rate filings, as well as in the recent local distribution cases before the Illinois Commission.
- *Allocators:* the use of a net, rather than a gross, plant allocator for the components of the accumulated deferred income taxes in Attachment 1, and for the real estate taxes in Attachment 2.[32]
- *Administrative and General:* ComEd has elected not to seek recovery of the salaries and benefits of certain officers of Exelon Corporation traditionally included in Administrative and General expenses.

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[31] *Citing Baltimore Gas & Elec.*, 115 FERC ¶ 61,066 (2006); *Duquesne*, 118 FERC ¶ 61,087(2007).

[32] ComEd states that an allocation of these costs on a net plant basis is consistent with the development of ComEd's distribution rates and is consistent with Commission precedent in *Northern Indiana Public Service Co., Inc.*, 101 FERC ¶ 61,394 at P 8 (2002).

- *Start Up Costs*: revisions to RTO start up costs approved in ComEd's last rate case, as explained in further detail below.

23. ComEd states that populating the formula with the most recent FERC Form 1 data results in a first year proposed gross annual transmission revenue requirement of $427.7 million, as compared to its existing revenue requirement of $297 million. ComEd explains that the reason for the increase is that its existing revenue requirement is based upon test year data that is 4 years old (2003), and since this time, ComEd has made $729 million in additional investment in its transmission plant, thereby substantially increasing its rate base above the existing 2003 plant in service.

24. ComEd requests an effective date of May 1, 2007, for its formula rate arguing that it would be injured greatly by a delay due to the significant costs it is experiencing from its investment in the West Loop and Grenshaw Projects. ComEd requests that the Commission approve the proposed formula rate without a hearing. Alternatively, ComEd requests that the Commission suspend the proposed formula rate for a nominal period to permit the requested May 1, 2007, effective date, and that the Commission specify the distinct issues or concerns that should be addressed in hearing or settlement proceedings.

II. Notice of Filings and Responsive Pleadings

A. Petition for Declaratory Order

25. Notice of ComEd's filing in Docket No. EL07-41-000 was published in the *Federal Register*, 72 Fed. Reg. 11,856 (2007), with interventions, protests and comments due on or before April 2, 2007.[33] The Illinois Commission filed a notice of intervention. Motions to intervene were timely filed by MidAmerican Energy Company, the City of Naperville, Illinois, Baltimore Gas and Electric Company, Illinois Municipal Electric Agency (IMEA), Mittal Steel USA Inc., Dominion Resources Services, Inc., Illinois Industrial Energy Consumers (IIEC), Old Dominion Electric Cooperative, PJM, PEPCO Holdings, Inc., Potomac Electric Power Company, Delmarva Power & Light Company, Atlantic City Electric Company, Northern Illinois Municipal Power Agency (NIMPA), and PPL Electric Utilities Corporation. Constellation Energy Commodities Group, Inc., Constellation NewEnergy, Inc., and Bluestar Energy Services, Inc filed motions to

[33] On March 20, 2007, the Illinois Commission filed a motion requesting an extension of time to file comments until April 18, 2007 in Docket Nos. EL07-41-000 and ER07-583-000. The Commission granted this motion on March 20, 2007. On March 26, 2007, ComEd filed comments stating that it continued to seek an effective date of May 1, 2007 for its proposed formula rate.

intervene out-of-time. NIMPA, IIEC, and IMEA filed protests. The Illinois Commission filed comments. IMEA filed a motion to consolidate the petition for declaratory order in Docket No. EL07-41-000 with the section 205 filing in Docket No. ER07-583-000. ComEd filed an answer opposing the motion to consolidate and filed an answer to the protests.

26. NIMPA argues that ComEd has not shown that the Projects are eligible for incentive rate treatment (*i.e*., by demonstrating that the Projects either enhance reliability or reduce the cost of delivered power by reducing transmission congestion).[34] IIEC contends that the West Loop and Grenshaw Projects did not result from a regional planning process and thus should not be afforded the rebuttable presumption of eligibility. Instead, IIEC argues that the Projects are both part of the Chicago Optimization Plan,[35] which resulted from investigations of outages that occurred in Chicago in the summer of 1999. IMEA claims that while the West Loop Project meets the rebuttable presumption that the project results from a regional planning process, the Grenshaw Project does not. IMEA argues that the Commission has found that TOI projects, such as the Grenshaw Project, cannot be presumed to have met the rebuttable presumption of eligibility for incentives.[36] IMEA requests that the Commission reject ComEd's petition. In the event the Commission does not reject the filing, IMEA requests that the Commission set it for hearing. IMEA also moves to consolidate the petition with ComEd's section 205 filing, stating that even if the Commission were to consider the incentives for ComEd's Projects, the Commission would still need to determine whether they are necessary in light of the formula rate proposal that ComEd seeks in its section 205 filing. ComEd answers that both of the Projects qualify for incentive rate treatment and that none of the arguments raised by protestors credibly refute this assertion.

27. Several parties argue that ComEd fails to demonstrate that there is a nexus between the incentives it seeks and the West Loop and Grenshaw Projects. IIEC states that ComEd is under a prior obligation to build the Projects as part of the Chicago Optimization Plan; thus, traditional ratemaking is appropriate since ComEd is simply meeting a prior commitment to improve reliability on the system. The Illinois

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[34] 18 C.F.R § 35.35(i) (2007).

[35] IIEC explains that this plan contains ComEd's proposed transmission solution to problems on its transmission and distribution system that it has committed to construct. IIEC states that the Chicago Optimization Plan was developed by ComEd long before ComEd even joined PJM. IIEC Protest at 4.

[36] IMEA Protest at 5 (*citing Duquesne*, 118 FERC ¶ 61,087 at P 66).

Commission concurs that because the Grenshaw Project is not voluntary and is instead pursuant to a binding agreement with the City of Chicago to construct this project, there is not a sufficient nexus since ComEd was required to construct and put into service on the same date, regardless of the Commission granting any sort of incentive rate treatment. ComEd disagrees with arguments that incentive rate treatment is not appropriate for the Projects because they are part of ComEd's "long-standing corporate commitment to improving reliability to the City of Chicago" and a "voluntary commitment that ComEd made to the City of Chicago."[37] ComEd states that Order No. 679 did not intend to deny incentives for projects undertaken by utilities that have long demonstrated their commitment to the goals of Order No. 679, while only "bribing" utilities that have not previously demonstrated a commitment to reliability.

28. Several parties state that ComEd has not shown how its transmission development program caused or contributed to the current pressure on its finances and resulted in a low grade credit rating for the company, and given the small scale of the Projects compared to ComEd's overall transmission investment, financing the Projects would likely have little impact on ComEd's overall credit rating. IIEC maintains that ComEd's credit rating downgrades have occurred due to regulatory uncertainty in Illinois with respect to its power procurement activities and not because of its transmission development programs.

29. IMEA argues that the Projects are not the sort of large, high-voltage, multi-state projects as those recently granted incentive rate treatment by the Commission;[38] instead, the West Loop and Grenshaw Projects are small, local projects designed only to meet local needs. IMEA also argues that these Projects do not require a significant financial investment or present financing challenges that ComEd would not face in the ordinary course of business. It states that in *Duquesne*, the proposed investment amounted to about 76 percent of the company's then current plant in service.[39] In comparison, Phase I of the West Loop Project, Phase II of the West Loop Project, and the Grenshaw Project amount to about 6 percent, 15 percent, and 3 percent, respectively, of ComEd's almost $1.69 billion total net transmission plant in service. ComEd answers that its Projects are not "routine" or "small, local projects designed to meet local needs" for "normal levels of

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[37] ComEd Answer at 10.

[38] IMEA Protest at 6 (*citing American Electric Power Service Corp.*, 116 FERC ¶ 61,059 (2006), *order on reh'g*, 118 FERC ¶ 61,041 (2007); *Allegheny Energy, Inc.*, 116 FERC ¶ 61,058 (2006), *order on reh'g*, 118 FERC ¶ 61,042 (2007)).

[39] IMEA Protest at 8 (*citing Duquesne*, 118 FERC ¶ 61,087 at P 52).

system reliability," because the Projects are major, complex projects that exceed NERC planning standards in order to provide a higher level of reliability to the business district of the City of Chicago, a vital population and financial center of national importance. ComEd argues that the Commission should dismiss IMEA's argument that the Projects are routine because they represent a lesser percentage of ComEd's total transmission plant in service when compared to that in *Duquesne*. ComEd states that its total net transmission plant is far greater than that in *Duquesne* and that ComEd is not seeking incentives for all of its baseline and TOI projects under the PJM RTEP.[40]

30. Finally, IMEA contends that ComEd faces no significant regulatory or technological risks, as there are no local/state approvals outstanding that may work to inflate the Projects' costs and that use of the new XLPE cables, standing alone, cannot suffice to establish a nexus.

31. Several protestors also argue that there is not a sufficient nexus between the proposed incentives and the completed Projects (*i.e*., Phase I of the West Loop Project and the Grenshaw Project) because the incentives would not be facilitating future investment. The Illinois Commission states that there is no rational basis for granting incentives to the Projects that have been completed and placed into service and notes that portions of the Projects were first approved 38 months before the passage of the EPAct 2005. The Illinois Commission also argues that Order No. 679 rejected applying incentive ROEs to existing transmission since such incentives would not improve reliability or reduce congestion and that similar reasoning should apply in the instant filing. IMEA maintains that ComEd's argument –that incentives are appropriate for the completed Projects because none of the associated costs have yet been recovered – is beside the point, as ComEd will receive full cost recovery for the Projects under its section 205 filing. NIMPA concurs that investors do not generally need the added comfort of an increased return to justify a proposed investment that has already occurred, regardless of whether the investment will be recovered. ComEd answers that the Grenshaw Project and Phase I of the West Loop Project should not be denied incentives just because the Projects have been placed in-service.

32. Several protestors argue that ComEd has a high assurance of cost recovery through traditional ratemaking. The Illinois Commission states that with respect to Phase II of the West Loop Project, which has not yet been placed into service, an incentive ROE is not appropriate since there is a tariff mechanism in ComEd's section 205 filing that will

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[40] ComEd asserts that the total projected costs of the Projects is $394 million, while the total cost in *Duquesne* for the eight baseline and 14 TOI projects is $118 million. ComEd Answer at 6-7.

allow ComEd to pass costs of the Projects on to its retail customers, thus recovering those investments through already-approved retail rate mechanisms. IMEA contends that ComEd's financial risks for the Projects are amply covered through the traditional DCF analysis, arguing that the proposed incentives are unnecessary in light of ComEd's proposed formula rate, which will materially advance ComEd's financial position. IMEA claims that ComEd fails to explain how the proposed incentives will appreciably aid its credit rating or cash flow in light of the requested formula rate and cost recovery guarantees in its section 205 filing. In its answer, ComEd argues that ComEd's proposed formula rate is not a form or request of incentive ratemaking, and is mischaracterized by protestors. Instead, ComEd contends that the proposed formula rate is independent of the requested incentives proposed in the petition.

B. Section 205 filing

33. Notice of ComEd's section 205 filing in Docket No. ER07-583-000 was published in the *Federal Register*, 72 Fed. Reg. 11,021 (2007), with interventions, protests and comments due on or before March 22, 2007.[41] The Illinois Commission filed a notice of intervention. Motions to intervene were timely filed by MidAmerican Energy Company, Baltimore Gas and Electric Company, IMEA, Wisconsin Electric Power Company, Allegheny Power, Mittal Steel USA, Inc., Dominion Resources Services, Inc., IIEC, Old Dominion Electric Cooperative, PJM, PEPCO Holdings, Inc., Potomac Electric Power Company, Delmarva Power & Light Company, Atlantic City Electric Company, City of Naperville, Illinois, NIMPA, and PPL Electric Utilities Corporation. Constellation Energy Commodities Group, Inc., Constellation NewEnergy, Inc., and Bluestar Energy Services, Inc filed motions to intervene out-of-time. NIMPA, IIEC, and IMEA filed protests. The Illinois Commission filed comments. IMEA filed a motion to consolidate the petition for declaratory order in Docket No. EL07-41-000 with the section 205 filing in Docket No. ER07-583-000. ComEd filed an answer opposing the motion to consolidate and filed an answer to the protests.

34. NIMPA argues that ComEd's proposed incentives are cumulatively unnecessary (adders on top of a proposal to impose a formula rate and recovery of 100 percent of CWIP). The IIEC states that ComEd's proposal to include CWIP in rate base should be rejected, since the transmission investments are not yet in service and ComEd's customers are not receiving benefits from the investments. The IIEC states that this will lower ComEd's revenue requirement by $11 million.

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[41] The Commission granted Illinois Commission's motion to extend the time to file comments until April 18, 2007.

35. IIEC states that ComEd's ROE is excessive, stating that it should be about 10 percent, considering today's low capital market costs. IIEC states that lowering the ROE would reduce ComEd's revenue requirement by $39 million.

36. Several parties protest ComEd's capital structure, stating that ComEd's requested 58.3 percent equity and 41.7 percent debt, as presented in its formula rate, was not what was approved by the Illinois Commission in Docket No. 05-0597.[42] IIEC states that this would reduce ComEd's revenue requirement by approximately $28 million.

37. The Illinois Commission argues that ComEd's proposed revenue requirement of $427.7 million is an approximately 44 percent increase from its existing revenue requirement of $296.7 million approved in 2003. The Illinois Commission requests the formula rates be suspended until after the 2007 summer cooling season.

38. The Illinois Commission notes that ComEd is using one-eighth of transmission operations and maintenance expenses as a cash working capital allowance without a lead/lag study.[43] The Illinois Commission states that this results in a cash working capital allowance of $11.8 million. The Illinois Commission requests that a lead/lag study be prepared before the Commission considers this aspect of the formula.

39. The Illinois Commission protests ComEd's formula rate proposal on the following issues and asks the Commission to carefully review the issues in the Illinois Commission Docket No. 05-0597: ComEd's proposal to automatically include prepayments for prepaid expenses[44] which results in an over-funded pension trust fund; adjustments to administrative and general (A&G) expenses; 2006 and 2007 Plant Additions;

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[42] The Illinois Commission notes that it accepted a capital structure of 42.86 percent equity and 57.14 percent debt.

[43] 18 C.F.R. 35.13(h)12. Statement AL requires utilities to file this statement establishing the need for cash working capital "to meet ongoing cash disbursements that must be made at time periods different than related revenue receipts for utility services rendered." Lead/lag studies are studies that show, in part, the average period between when the utility pays the expense, and when the utility receives revenues attributable to such service. These studies are acceptable demonstrations of the need for cash working capital to pay expenses in time periods different than the related revenue receipts for utility services rendered.

[44] The Illinois Commission cites ComEd's section 205 filing, Appendix C, Exhibit No. CWE-103 at 3.

depreciation additions; CWIP; excessive ROE; formula rate protocols for interested parties to challenge annual updates; and interested parties' filing rights under section 206 of the FPA (section 206 filing rights).[45]

III. Deficiency Letter, Notice of Amended Filing, and Responsive Pleadings

40. On March 30, 2007, the Commission issued a deficiency letter directing ComEd to provide the following information: (i) a description of the incentive Projects by PJM Project Identification Number and incentives requested; (ii) a demonstration of the reliability issues that the Grenshaw Project addresses, inclusive of reliability violations for the short and long-term planning horizon, and a nexus between the project and the incentive sought; (iii) a description of the specific benefits of the XLPE cable to address demonstrable risks or challenges faced, by PJM Project Identification Number; (iv) description of advanced transmission technologies used in the incentive Projects; (v) an explanation of whether any of the Projects are required as a result of an order or requirement from a regulatory body, government body, or regional entity; (vi) a revenue increase disclosure inclusive of the requested ROE adders; (vii) an explanation of RTO start up costs, including an explanation of how these costs are non-recurring, and distinct from previously-approved RTO start-up costs;[46] (viii) an explanation of the $776 million in "goodwill impairment" recorded in ComEd's formula rate, including an explanation of why this item will not be deducted from rate base, and how it will be recorded in future Form 1 balances; (ix) a revenue increase disclosure for the formula rates; (x) an explanation of whether the tax benefits resulting from ComEd's effective income tax rate of negative 116 percent have been incorporated in the proposed formula rate common equity calculations as equity capital contributions or in some other form; and (xi) an explanation for the deviation from the Commission's policy in *San Diego Gas & Electric Co.*,[47] which requires an average of 13 monthly balances for transmission-related balances.

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[45] Illinois Commission Protest at 18-23.

[46] In *Commonwealth Edison Co.*, 105 FERC ¶ 61,186 (2003), *accepting uncontested settlement*, 109 FERC ¶ 61,338 (2004), the Commission approved ComEd's use of a ten-year amortization period and proposed carrying charge for both Alliance and PJM start up costs of $8,242,898. This approval was in addition to the $10,730,903 of start up costs included for recovery in Docket No. ER03-262-000.

[47] 118 FERC ¶ 61,073 (2007) at P 29, *reh'g pending*.

41. On April 12, 2007, ComEd amended its filing by submitting its response to the deficiency letter. ComEd clarifies that it is seeking incentives only for two Projects, the West Loop and Grenshaw Projects, not all of the projects contained in the PJM RTEP. ComEd responds that each of the Projects, including the completed Grenshaw Project and Phase I of the West Loop Project, satisfy the temporal requirement for eligibility of incentives under Order No. 679 because they were placed into service after August 8, 2005. ComEd states that it could not submit its petition until Order No. 679 became effective in September 2006. ComEd argues that the Commission has not adopted a bright line based on construction completion dates in rulings submitted pursuant to Order No. 679 and notes the Commission's conditional approval of the proposed incentives in *Duquesne*, which included approximately $18 million in investment associated with completed projects.

42. In its deficiency response, ComEd explains that it had a binding commitment with the City of Chicago to construct the facilities by a date certain, as part of a comprehensive discussion with the City of Chicago on reliability and franchise issues.

43. ComEd also reconciled discrepancies in its calculation of the rate impact of the incentive ROE adder, noting that the increase in its revenue requirement due to the requested 150 basis point adder would result in $5,143,086 increase in the overall revenue requirement annually.

44. ComEd explains the additional RTO start-up costs, stating that they are legal and/or consulting fees associated with several ongoing proceedings that are a direct result of ComEd's integration into PJM,[48] and that none of these costs have been recovered in prior filings.

45. ComEd additionally represents that its prior revenue requirement of $296.7 million is based upon a 2003 test year. ComEd states that the proposed $427.7 million revenue requirement in the section 205 filing results in an increase of $131 million from its prior revenue requirement. ComEd states that the increase is due to substantial transmission plant investments since 2003.

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[48] ComEd deficiency response at 11-13. ComEd cites the following proceedings: (1) Docket Nos. ER04-364-000, ER04-375-000 (utilities in Wisconsin and Michigan be held harmless from loop flow or congestion resulting from ComEd's participation in PJM); (2) ER05-6-000, EL04-135-000, EL02-111-000, EL03-212-000 (FERC's investigation into through-and-out rates of the Midwest Independent System Operator, Inc., (Midwest ISO) and PJM); and (3) ER03-262-000 (related to the original application of ComEd and others to join PJM), and other costs.

46. Notice of ComEd's deficiency response filing was published in the *Federal Register*, 72 Fed. Reg. 20,519, with interventions, protests and comments due on or before April 27, 2007. The Illinois Commission filed comments as identified above.

IV. Discussion

A. Procedural Matters

47. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure,[49] the notices of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to the proceedings in which they were filed. We will grant Constellation Energy Commodities Group, Inc., Constellation NewEnergy, Inc., and Bluestar Energy Services, Inc.'s untimely motions to intervene, given their interest in this proceeding, the early stage of the proceeding, and the absence of any undue prejudice or delay.

48. Rule 213(a) of the Commission' Rules of Practice and Procedure[50] prohibits an answer to a protest and an answer to an answer, unless otherwise permitted by the decisional authority. We will accept ComEd's answer to the protests in Docket No. EL07-41-000 because it provided information that assisted us in our decision-making process. We are not persuaded to accept ComEd's answer to protests in Docket No. ER07-583-000 and will, therefore, reject it.

49. IMEA's motion to consolidate Docket Nos. EL07-41-000, ER07-583-000, and ER07-583-001 for purposes of hearing is moot, since we deny ComEd's petition requesting incentive rate treatment as discussed below.

B. Request for Transmission Incentives

1. Section 219 Requirements

50. In EPAct 2005, Congress addressed the allowance of incentive-based rate treatments for new transmission construction.[51] Specifically, section 1241 of EPAct 2005 added new section 219 to the FPA, directing the Commission to establish, by rule, incentive-based (including performance-based) rate treatments. The Commission issued

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[49] 18 C.F.R. § 385.214 (2007).

[50] *Id.* § 385.213(a)(2).

[51] *See* Pub L. No. 109-58, § 1241, 119 Stat 594, 961 (2005).

Order No. 679, which set forth processes by which a public utility could seek transmission rate incentives pursuant to section 219, including the incentives requested here by ComEd.

51. Order No. 679 provided that a public utility may file under the FPA a petition for declaratory order or a section 205 filing to obtain incentive rate treatment for transmission infrastructure investment that satisfies the requirements of section 219, *i.e.*, the applicant must demonstrate that the facilities for which it seeks incentives either ensure reliability or reduce the cost of delivered power by reducing transmission congestion.[52] Order No. 679 established the rebuttable presumption that an investment meets the requirements of section 219, thus qualifying for transmission incentives, if the applicant demonstrates either that: (i) the transmission project results from a fair and open regional planning process that considers and evaluates projects for reliability and/or congestion and is found to be acceptable to the Commission; or (ii) a project has received construction approval from an appropriate state commission or state siting authority."[53] Order No. 679-A also clarified the operation of this rebuttable presumption by noting that the authorities and/or processes on which it is based (*i.e.*, a regional planning process, a state commission, or siting authority) must, in fact, consider whether the project ensures reliability or reduces the cost of delivered power by reducing congestion.[54]

52. We find that for the West Loop Project, ComEd has met the section 35.35(i) rebuttable presumption for incentive rate treatment in that: (i) the West Loop Project has been approved and received certificates of public convenience and necessity from the Illinois Commission, and (ii) the West Loop Project has been identified as a baseline project within the PJM RTEP.

2. <u>Incentives and the Commission's Nexus Requirement</u>

53. In addition to satisfying this section 219 requirement, a proposed incentive rate must also be shown to have a nexus between the incentive sought and the investment being made. The Commission stated that in evaluating whether an applicant has satisfied the required nexus test, the Commission will examine the total package of incentives being sought, the inter-relationship between any incentives, and how any requested

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[52] *See* 18 C.F.R. § 35.35(i) (2007).

[53] *See id.*; Order No. 679-A, 117 FERC ¶ 61,345 at P 47.

[54] Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 49.

incentives address the risks and challenges faced by the project.[55] Applicants must provide sufficient explanation and support to allow the Commission to evaluate the incentives. In addition, the Commission has clarified that it retains the discretion to grant incentives that promote particular policy objectives, unrelated to whether or not a project presents specific economic risks or challenges.[56]

54. In Order No. 679-A, the Commission clarified that its nexus test is met when an applicant demonstrates that the total package of incentives requested is "tailored to address the demonstrable risks or challenges faced by the applicant."[57] By its terms, this nexus test is fact-specific and requires the Commission to review each application on a case-by-case basis.[58]

55. As discussed herein, we find that ComEd has not satisfied the Commission's "nexus" requirement for the Projects, and therefore, we reject the proposed incentives, and deny ComEd's petition for declaratory order.

56. Order No. 679 states that the Commission will "consider applications for ROE incentives for all projects," but that the "the most compelling case for incentive ROEs are new projects that present special risks of challenges, not "routine investments made in the ordinary course" of business.[59] Here, ComEd states that these Projects constitute "the most expensive and complex transmission infrastructure investment ever made by ComEd…"[60] ComEd also states that the cost associated with the West Loop Project, along with the recently completed Grenshaw Project, is roughly equivalent to the entire cost incurred for all transmission plant additions over the four-year period from 2001-2004. ComEd provides no data in its petition and section 205 filing to support these statements. Rather, ComEd supplies data that appears to contradict these statements.

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[55] 18 C.F.R. § 35.35(d) (2007); Order No. 679, 116 FERC ¶ 61,057 at P 26. *See also* Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 21 ("By this we mean that the incentive(s) sought must be tailored to address the demonstrable risks and challenges faced by the applicant in undertaking the project.")

[56] Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at n.37.

[57] *Id.* P 40.

[58] *See* Order No. 679, *order on reh'g*, 119 FERC ¶ 61,062 at P 18.

[59] Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 60.

[60] ComEd petition, Attachment A at P 5.

57. Indeed, ComEd's filing gives the impression that its transmission additions from 2005-2008 (the time period of the Projects, at a combined cost of $393 million for the Projects) are roughly equivalent to its transmission additions from 2001-2004, which would imply that the Projects are of a routine nature. Contrary to its statements indicating the enormous investment of the Projects, ComEd acknowledges that it has included $729 million in new transmission investment since 2003, *not including* the Projects.[61] ComEd provides no additional data to compare the cost of the Projects to other costs. The information provided suggests that ComEd is making an investment consistent with what it has routinely undertaken.

58. In addition, ComEd presents that its Transmission Plant In-Service is $1.68 billion.[62] Comparatively, the remaining investment need for Phase II of the West Loop Project is $250 million. ComEd's remaining investment need is roughly 14 percent of its current net transmission plant in service.[63] ComEd has not sufficiently demonstrated how this comparatively small investment can be argued to pose a special risk for a company the size of ComEd.

59. Under the unique facts of this case, we conclude that, ComEd's capital outlay is well within the category of "routine investments made in the ordinary course" as discussed in Order No. 679-A.[64] Order No. 679 states that "Ordinarily, such an incentive would be appropriate for large new investments or in situations, as occurred with *ATC*, where denying such an incentive would adversely affect the utility's ratings."[65] Order No. 679 further states that "[a]llowing public utilities the opportunity, in appropriate situations, to include 100 percent of CWIP in the calculation of transmission rates and to expense pre-commercial operations costs for new transmission investment (instead of capitalizing these costs and earning a return) removes a disincentive to construction of transmission, which can involve very long lead times and considerable risk to the utility that the project may not go forward."[66] However, as explained below, these circumstances are not present in the case of ComEd's Projects.

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[61] ComEd section 205 filing at 7; ComEd petition at 19.

[62] As presented in ComEd petition, Attachment D-1 at 4, line 179.

[63] ComEd petition, Attachment D-1 at 4, line 179.

[64] Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 60.

[65] *Id.* P 116.

[66] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 117.

60. Nothing in the record demonstrates that granting ComEd a higher authorized ROE for its project will measurably assist ComEd in financing its Projects, and help preserve its credit quality, for such a comparatively small project. Further, ComEd's statements that the requested incentives are needed for cash flow conflict with ComEd's recent actions. Specifically, ComEd has been able to prematurely retire long-term debt in recent years, and attract as much as $1 billion in revolving credit as recently as February 2006.[67]

61. Order No. 679 also states that, "Given the long lead time required to construct new transmission, and the associated cash flow difficulties faced by many entities wishing to invest in new transmission, the Final Rule provides that, where appropriate, the Commission will allow for the recovery of 100 percent of CWIP in rate base." Such is not the case with ComEd, where the Project completion date is 2008, and it has demonstrated an ability to retire significant amounts of debt, and attract investment as recently as February 2006.

62. Order No. 679 requires that companies seeking an incentive ROE demonstrate "why it is appropriate to encourage new investment."[68] Particularly, in Order No. 679-A, we stated that "…we are obligated to establish ROEs for public utilities that both reflect the *financial* and *regulatory* risks (emphasis added) attendant to a particular project and that are sufficient to actively promote capital investment."[69]

63. Under the unique facts of this case, ComEd has not demonstrated that it is presented with a regulatory risk attendant to the Projects for which it seeks incentives. All of the necessary regulatory approvals have been received for the Projects, and the investment in the Projects have the ability to be recovered through traditional ratemaking.

64. As stated above, based on the unique facts of this case, ComEd has not demonstrated that it faces financial risks associated with the Projects, since ComEd has achieved financing, has an investment-grade rating, and has not provided a cash flow analysis to demonstrate that its credit rating will be negatively impacted. ComEd's contention that the incentives are needed to ensure financing or speed completion of the Projects is not supported by the fact that two of the Projects are completed and the third project will be completed next year.

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[67] As filed in ComEd's FERC Form 1 (2006) at 121.72 and 109.2.

[68] Order No. 679, FERC Stats. & Regs. ¶ 31,222 at P 219.

[69] Order No. 679-A, FERC Stats. & Regs. ¶ 31,236 at P 15.

65. When compared to the Commission's criteria outlined in Order No. 679, and as Order No. 679's criteria were applied in *Duquesne*, ComEd falls well short of several marks that Duquesne had met. For example, in *Duquesne*, the Commission found that the project was not routine in terms of the amount of investment it would require. Duquesne's investment was "$184 million, which is roughly 76 percent of its current net transmission plant in service." Further, Duquesne's projects required Duquesne to make annual transmission plant expenditures over the next several years that will be approximately eighteen times its average expenditures over the last five years.[70]

66. This is not the case with ComEd's Projects, where the total investment is only 14 percent of ComEd's net transmission plant, and is not multiples of, but equivalent to, the amount of expenditures it has made over four years (from 2001-2004).

67. In *Duquesne*, the Commission found that the incentives were needed to maintain cash flow to complete the projects. Specifically, we found that without the incentives, "…Duquesne could experience deterioration in its credit quality that could lead to higher rates and commitment fees under its current revolving credit facility, in addition to increasing its borrowing costs under any new long-term borrowing arrangements." [71]

68. However with ComEd, incentives are not needed to maintain its credit quality, and it has not made any demonstration that without the incentives, its financial condition will weaken. Further, ComEd has not sufficiently shown that the incentives are needed to maintain cash flow, particularly in light of its recent financial activity.

69. In *Duquesne*, the Commission found that Duquesne had not received all of the necessary siting approvals yet, which introduced and increased regulatory risk, thereby meriting the higher ROE.[72] Here, ComEd has received all of the necessary regulatory approvals and there is thus no regulatory risk.

70. For the reasons discussed above, the Commission finds that ComEd has not sufficiently demonstrated the required nexus pursuant to Order No. 679 for the incentive ROE adder or for CWIP inclusion in rate base. Therefore, ComEd's request for a 150 basis point adder for the Projects and its proposal to include 100 percent of CWIP in rate base for Phase II of the West Loop Project are denied.

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[70] *Duquesne*, 118 FERC ¶ 61,087 at P 52.

[71] *Id*. P 59.

[72] *Id.* P 54.

71. Based on the evidence and support provided by ComEd, we cannot find that ComEd's total package of incentives satisfies the Commission's nexus requirement. However, ComEd's proposal to use underground XLPE cable at 345 kV as part of Phase II of the West Loop Project may be similar to the use of advanced transmission technologies proposed by the United Illuminating Company (UI) in Docket No. ER07-653-000, where UI requested a 50 basis point adder for advanced transmission technologies.[73] It is not clear whether ComEd has requested a rate incentive for its use of an advanced transmission technology, but in any case, ComEd has not provided sufficient support for the Commission to grant a rate incentive for the use of advanced technology. Our denial of incentives for the Projects is without prejudice to ComEd making a future filing that is fully supported for a rate incentive based on its use of advanced technologies.

C. Formula Rate

72. For the reasons discussed below, we will accept ComEd's proposed formula rate and 50 basis point adder for RTO participation, subject to conditions and nominal suspension, hearing, and settlement judge procedures, effective May 1, 2007, as requested, subject to refund.

1. Hearing and Settlement Judge Procedures

73. ComEd's proposed formula rate raises issues of material fact that cannot be resolved based on the record before us, and are more appropriately addressed in the hearing and settlement judge procedures ordered below.

74. Our preliminary analysis of the components of ComEd's proposed formula rate, including ComEd's proposed 11.7 percent ROE and certain other elements of ComEd's filing as discussed below, indicate that these components of the proposed formula have not been shown to be just and reasonable and may be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful. Therefore, we will conditionally accept ComEd's proposed formula rate for filing, suspend it for a nominal period, make it effective May 1, 2007, subject to refund, and set specific issues for hearing and settlement judge procedures.

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[73] *See The United Illuminating Co.*, 119 FERC ¶ 61,182 (2007).

75. In *West Texas Utilities Company*,[74] the Commission explained that when its preliminary examination indicates that the proposed rates may be unjust and unreasonable, and may be substantially excessive, as defined in *West Texas*, the Commission would generally impose a five-month suspension. It is recognized, however, that shorter suspensions may be warranted in circumstances where suspension for the maximum period may lead to harsh and inequitable results.[75] Such circumstances exist here where the Commission has, in fact, urged transmission owners to move from stated rates to formula rates, and where customers would also benefit from the incentive provided by these rate changes to ComEd to commence construction of RTEP upgrades. Accordingly, the Commission will exercise its discretion to suspend the revisions to the ComEd's rates for a nominal period and permit the rates to become effective May 1, 2007, subject to refund and the outcome of the hearing established in this order.

76. As noted above, protesters raise numerous issues regarding the reasonableness of the proposed rates that are best addressed in the hearing we order below. At the hearing, ComEd will be required to support and justify the justness and reasonableness of its proposal.

77. First, we set for hearing ComEd's proposed base 11.7 percent ROE, including the composition of its proxy group, capital structure, and related ROE issues. The 50 basis point ROE incentive approved for RTO participation (bringing the overall requested ROE to 12.2 percent) will be bounded by the upper end of the zone of reasonableness determined at hearing. With respect to its proposed proxy group, ComEd proposes to include American Electric Power Corp., Consolidated Edison, Inc, Constellation Energy Group, Dominion Resources, Inc., DPL, Inc., Energy East Corp., Exelon Corp., FirstEnergy Corp., FPL Group, Inc., Northeast Utilities, NSTAR, Pepco Holdings, Inc., PPL Corp., Public Service Enterprise Group, Inc., and UIL Holdings Corporation.[76] Certain of these companies own transmission assets within the PJM system (*i.e.*, American Electric Power Corp., Consolidated Edison, Inc., Constellation Energy Group, Dominion Resources, Inc., DPL, Inc., Exelon Corp., FirstEnergy Corp., Pepco Holdings Inc., PPL Corp., and the Public Service Enterprise Group, Inc.) and therefore may be regarded as presumptively representative companies in terms of their overall risk profiles. However, the other companies relied upon by ComEd (*i.e.*, Energy East Corp., NSTAR

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[74] 18 FERC ¶ 61,189 at 61,374 (1982) (*West Texas*).

[75] *California Independent System Operator Corp.*, 105 FERC ¶ 61,406 (2003), *order on reh'g*, 107 FERC ¶ 61,048 (2004).

[76] ComEd section 205 filing, Appendix D, Exhibit. No. CWE-201 at 1.

and UIL Holdings, Northeast Utilities, and FPL Group, Inc.) do not own transmission assets within PJM.

78. In *Midwest Independent Transmission System Operator, Inc.*,[77] the Commission accepted a proxy group of Midwest ISO transmission owners in setting an ROE applicable to the participating transmission owners in the Midwest ISO.[78] Applying this precedent here, ComEd has not shown that its proposal to include in its proxy group companies that have no direct link to PJM to be just and reasonable.

79. We will permit, however, participants in the hearing to consider the appropriateness of including or excluding particular PJM transmission owners from the proxy group. We will also permit ComEd and other participants to demonstrate that companies with no direct link to PJM should be included in ComEd's proxy group. However, we do not expect such companies to be included in ComEd's proxy group unless there is compelling evidence to support a deviation from our general policy of requiring a proxy group to be comprised of transmission owners with a direct link to the same RTO or ISO in which the applicant is located.

80. We also set for hearing: (i) the formula's use of end of year values for prepaid expenses and materials and supplies in rate base;[79] (ii) the $776 million adjustment to reflect goodwill impairment as a result of its annual impairment assessment of long-lived assets under FAS 144;[80] (iii) the $23.8 million of transmission-related Electric Plant Held for Future Use in rate base;[81] (iv) the use of the Gross Revenue Requirement in developing the Net Plant Carrying Charge[82] which over-recovers costs by including, *e.g.*, revenue credits from Attachment 3 of the formula and direct-assignment interconnection costs that have already been paid for by interconnection customers through other rate

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[77] 100 FERC ¶ 61,292 (2002) (*Midwest ISO ROE Order*), *order on reh'g*, 102 FERC ¶ 61,143 (2003), *order on remand*, 106 FERC ¶ 61,302 (2004), *aff'd*, *Public Service Comm'n of Kentucky v. FERC*, 397 F.3d 1004 (D.C. Cir. 2005).

[78] *See Midwest ISO ROE Order*, 100 FERC ¶ 61,292 at P 32.

[79] ComEd section 205 filing, Appendix C, Exhibit No. CWE-103 at 2, line 61.

[80] *Id.* at lines 19, 36, 117 (referencing Note Q).

[81] *Id.* at line 34.

[82] *Id.* at line 173.

schedules consistent with Order No. 2003-A;[83] (v) ComEd's proposal to automatically include prepayments for prepaid expenses[84] which results in an over-funded pension trust fund; (vi) adjustments to A&G expenses; (vii) 2006 and 2007 Plant Additions; (viii) depreciation additions; (ix) cash working capital calculations; and (x) formula rate protocols for interested parties to challenge annual updates and interested parties' section 206 filing rights.

81. While we are setting the matters noted above for a trial-type evidentiary hearing, we encourage the parties to make every effort to settle their disputes before hearing procedures are commenced. To aid the parties in their settlement efforts, we will hold the hearing in abeyance and direct that a settlement judge be appointed, pursuant to Rule 603 of the Commission's Rules of Practice and Procedure.[85] If the parties desire, they may, by mutual agreement, request a specific judge as the settlement judge in the proceeding; otherwise, the Chief Judge will select a judge for this purpose.[86] The settlement judge shall report to the Chief Judge and the Commission within 60 days of the date of this order concerning the status of settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions or provide for commencement of a hearing by assigning the case to a presiding judge.

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[83] *Standardization of Generator Interconnection Agreements and Procedures*, Order No. 2003, 68 Fed. Reg. 49,845 (Aug. 19, 2003), FERC Stats. & Regs. ¶ 31,146 (2003), *order on reh'g*, Order No. 2003-A, 69 Fed. Reg. 15,932 (Mar. 26, 2004), FERC Stats. & Regs. ¶ 31,160 at P 657 (2004), *order on reh'g*, Order No. 2003-B, 70 Fed. Reg. 265 (Jan. 4, 2005), FERC Stats. & Regs. ¶ 31,171, *order on reh'g*, Order No. 2003-C, 70 Fed. Reg. 37,661 (June 30, 2005), FERC Stats. & Regs. ¶ 31,190 (2005), *aff'd sub nom. Nat'l Ass'n of Regulatory Util. Comm'rs v. FERC*, 475 F.3d 1277 (D.C. Cir. 2007). *See also* ComEd section 205 filing, Appendix C, Exhibit No. CWE-103 at n.N.

[84] The Illinois Commission cites ComEd's section 205 filing, Appendix C, Exhibit No. CWE-103 at 3.

[85] 18 C.F.R. § 385.603 (2007).

[86] If the parties decide to request a specific judge, they must make their joint request to the Chief Judge by telephone at (202) 502-8500 within five days of this order. The Commission's website contains a list of Commission judges and a summary of their background and experience (www.ferc.gov – click on Office of Administrative Law Judges).

2. Specific Findings

82. We make specific findings on the following issues:

(a) Capital Structure

83. ComEd proposes in its formula rate to reflect its actual capital structure derived from its Form 1 Accounts, consistent with Commission precedent. Protestors have not made a sufficient showing as to why the Illinois Commission capital structure applies in this case. ComEd's approach using the Company's Form 1 data is consistent with Commission precedent for PJM Transmission Owners with this type of formula rate, and will closely follow ComEd's actual capital structure.[87] We therefore accept ComEd's formula capital structure.

(b) Plant Allocators

84. ComEd is directed to remove from its formula rate the methodology for inclusion of CWIP in both the Gross Plant Allocator and Net Plant Allocator[88] which has the effect of overstating costs assigned to the transmission function. While there will be zero balances in the line items for CWIP in the formula, the formula contains provisions which have the effect of automatically including CWIP in these allocators, should CWIP in rate base ever be approved for future projects. We direct ComEd to remove the provisions of the formula which permit any future inclusion of CWIP.

(c) 50 Percent CWIP in Rate Base for All New Transmission Investment.

85. The Commission will not treat ComEd's request for inclusion of 50 percent CWIP in rate base as a formal incentive, but rather, pursuant to Order No. 298, such treatment is

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[87] All of the PJM transmission owners with this type of formula rate calculate their capital structures based upon actual data in their FERC Form No. 1. *See* Baltimore Gas & Electric Co., Atlantic City Electric Co., Delmarva Power & Light Co., Potomac Electric Power Co., Commonwealth Edison Company (pending in Docket No. ER07-583-000, *et al.*) and UGI Utilities, as filed in their formula rates under the PJM OATT, FERC Electric Tariff, Sixth Rev. Vol. No. 1, Att. H-18.

[88] ComEd section 205 filing, Appendix C, Exhibit No. CWE-103 at lines 16 and 18.

intended to act as an offset to the bias against new investment, among other things.[89] Notwithstanding this, ComEd has not made the *prima facie* case for a blanket approval of 50 percent CWIP in rate base for all transmission investment. Order No. 298 listed several conditions the requesting party must fulfill before receiving approval of this request.[90] For example, the party must demonstrate that any individual rate filing must not propose more than a six percent CWIP-related rate increase in the first year of the rule and no more than a 12 percent CWIP-related rate increase over the first two years.

86. Order No. 298 also required, *inter alia*, Statement BM, Construction Program Statement to be filed with the Commission. This statement requires a utility to describe its long-range program for providing reliable and economic power, to include an assessment of the relative costs of adopting alternative strategies, and to provide an explanation of why the program adopted is prudent and consistent with a least-cost energy supply program. Requiring this information is consistent with Commission policy.[91]

87. ComEd does not provide the necessary information for its request of 50 percent CWIP in rate base for all transmission investment, likely because the nature of Order No. 298's requirements for CWIP inclusion makes providing such information for an indefinite period of time for unspecified construction projects difficult, if not impossible.

88. While not all requests for including CWIP in rate base in the past have been for a specific project, previous requests would at least provide a timeline (*e.g*., ten years) during which the company had tangible and specific construction goals to improve its system.[92] For example, American Transmission Company proposed to modify its formula rate with the inclusion of CWIP in rate base as one way to facilitate the financing of approximately $2.3 to $2.8 billion in new transmission construction over a ten-year

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[89] *Boston Edison Co.*, 109 FERC ¶ 61,300 at P 32 (2004), *order on reh'g*, 111 FERC ¶ 61,266 (2005) (*Boston Edison*).

[90] Order No. 298, FERC Stats. & Regs. ¶ 30,455 at 30,534.

[91] *See* Order No. 298, FERC Stats. & Regs. ¶ 30,455. *See also Boston Edison*, 109 FERC ¶ 61,300; *American Transmission Co., L.L.C.*, 105 FERC ¶ 61,388 (2003) (*ATC I*), *order approving settlement*, 107 FERC ¶ 61,117 (2004) (*ATC II*); *Northeast Utilities Services Co.*, 114 FERC ¶ 61,089 (2006).

[92] *See ATC I*, 105 FERC ¶ 61,388.

period. American Transmission Company also provided a Net Present Value analysis that demonstrated that its requested inclusion of CWIP would actually lower rates for consumers during that time period.

89. ComEd's request in this matter provides neither a specific construction project for which it seeks to include 50 percent CWIP in rate base, nor does it detail a definitive time period during which multiple projects are planned. Rather, ComEd seeks indefinite permission to include 50 percent of CWIP in rate base for all transmission investment.

90. ComEd's filing fails to demonstrate that it fulfills the requirements for inclusion of CWIP in rate base when requesting a blanket CWIP proposal. Accordingly, we reject ComEd's request for a blanket inclusion of 50 percent CWIP in rate base for all transmission investment.

(d) <u>Waivers</u>

91. ComEd seeks a waiver of certain filing requirements relating to its recovery of Post-Employment Benefits Other Than Pension (PBOP) costs.[93] Specifically, ComEd proposes that any PBOP-related changes to its formula rate falling below a stated threshold (i.e., that do not exceed an impact on the formula output of its Net Zonal Revenue Requirement of $0.05 per kW-month, as compared to the immediately preceding Annual Update), be included in its Annual Update without the need to make a FPA section 205 or 206 filing.[94] We reject this provision of ComEd's proposal, as inconsistent with Commission Policy on PBOPs.[95] PBOP accounts are typically amounts that are amortized over a set period of time,[96] much like depreciation or decommissioning expenses.[97] A modification in the amortization without Commission scrutiny can result

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[93] *See Statement of Financial Accounting Standards No. 106*, Employers' Accounting for Postretirement Benefits Other Than Pensions.

[94] As proposed in PJM Interconnection, L.L.C., FERC Electric Tariff, Sixth Rev. Vol. No. 1, Original Sheet No. 314I.26, section 1(g).

[95] *See Maine Yankee Atomic Power Co*. 66 FERC ¶ 61,375, *order providing clarification*, 68 FERC ¶ 61,190 (1994).

[96] In accordance with Statement of Financial Accounting Standards No. 106.

[97] We note that depreciation rates must also be stated, but ComEd does not request any modification to its existing depreciation rates consistent with 18 C.F.R. § 35.13(h)(1)(iv) (2007).

in over-recovery or intergenerational inequities. ComEd is directed to submit revised tariff sheets reflecting this revision as part of the compliance filing to be made within 30 days of the date of this order.

92. Further, ComEd requests several waivers from the requirements of section 35.13 and 35.25 of the Commission's regulations (Filing of Changes in Rate Schedules). These include: (i) waiver of the full Period I/Period II data requirements;[98] (ii) waiver of the attestation concerning Period II submissions;[99] (iii) waiver of the requirement to determine if, and the extent to which, a proposed change constitutes a rate increase based on Period I/Period II rates and billing determinants;[100] and (iv) waiver of the cost of service statements. In support of its requested waivers, ComEd states that the cost support matrix and supporting worksheets with testimony accompanying its filing here provide ample support for the reasonableness of its proposed formula rate.

93. We deny ComEd's request for waiver of filing an attestation as required in 18 C.F.R.35.13(d)6. ComEd has provided no justification for the requested waiver. We will require ComEd to provide this attestation as part of its compliance filing to be made within 30 days of the date of this order, along with corrected tariff sheets reflecting the Commission's policy on PBOP.

94. However, we will grant the remaining waivers consistent with our prior approval of formula rates.[101] Nonetheless, to the extent that parties at the hearing procedures ordered below can show the relevance of additional information needed to evaluate this proposal, the presiding judge can provide for appropriate discovery of such information.

<u>The Commission orders</u>:

(A) ComEd's petition for a declaratory order in Docket No. EL07-41-000 is hereby denied, as discussed in the body of this order.

(B) ComEd's proposed formula rate in Docket Nos. ER07-583-000 and ER07-583-001 is hereby conditionally accepted for filing and suspended for a nominal suspension, to become effective May 1, 2007, as requested, subject to refund, subject to

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[98] 18 C.F.R. §§ 35.13(d)(1)-(2) (2007).

[99] *Id*. § 35.13(d)(6).

[100] *Id*. § 35.13(a)(2)(iv).

[101] *Baltimore Gas & Elec.*, 115 FERC ¶ 61,066 at P 55.

conditions and the outcome of hearing and settlement judge procedures, and subject to the compliance filing ordered in Ordering Paragraph (C), as discussed in the body of this order.

(C) ComEd is hereby directed to submit a compliance filing reflecting the rejection of certain requests for waivers within 30 days, as discussed in the body of this order.

(D) ComEd's request for waiver of the requirement of section 35.13 to provide full Period I and Period II data, and waiver of sections 35.13(a)(2)(iv); 35.13(d)(1) and (2), and section 35.13(h) is hereby granted.

(E) Pursuant to the authority contained in and subject to the jurisdiction conferred upon the Commission by section 402(a) of the Department of Energy Organization Act and the Federal Power Act, particularly sections 205 and 206 thereof, and pursuant to the Commission's Rules of Practice and Procedure and the regulations under the Federal Power Act (18 C.F.R. Chapter I), a public hearing shall be held concerning ComEd's proposed base-level ROE, as discussed in the body of this order. However, the hearing shall be held in abeyance to provide time for settlement judge procedures, as discussed in Paragraphs (F) and (G) below.

(F) Pursuant to Rule 603 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.603 (2004), the Chief Administrative Law Judge is hereby directed to appoint a settlement judge in this proceeding within fifteen (15) days of the date of this order. Such settlement judge shall have all powers and duties enumerated in Rule 603 and shall convene a settlement conference as soon as practicable after the Chief Judge designates the settlement judge. If the parties decide to request a specific judge, they must make their request to the Chief Judge in writing or by telephone within five (5) days of the date of this order.

(G) Within thirty (30) days of the appointment of the settlement judge, the settlement judge shall file a report with the Commission and the Chief Judge on the status of the settlement discussions. Based on this report, the Chief Judge shall provide the parties with additional time to continue their settlement discussions, if appropriate, or assign this case to a presiding judge for a trial-type evidentiary hearing, if appropriate. If settlement discussions continue, the settlement judge shall file a report at least sixty (60) days thereafter, informing the Commission and the Chief Judge of the parties' progress toward settlement.

(H) If settlement judge procedures fail and a trial-type evidentiary hearing is to be held, a presiding judge, to be designated by the Chief Judge, shall, within fifteen (15)

days of the date of the presiding judge's designation, convene a prehearing conference in this proceeding in a hearing room of the Commission, 888 First Street, N.E., Washington, D.C. 20426. Such conference shall be held for the purpose of establishing a procedural schedule. The presiding judge is authorized to establish procedural dates, and to rule on all motions (except motions to dismiss) as provided in the Commission's Rules of Practice and Procedure.

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.