

BEFORE THE ARKANSAS PUBLIC SERVICE COMMISSION

**IN THE MATTER OF THE APPLICATION OF)
AEP SOUTHWESTERN TRANSMISSION)
COMPANY, INC. FOR RECOGNITION AS A)
PUBLIC UTILITY WITH POWERS OF EMINENT)
DOMAIN AND CERTIFICATED FOR THE)
PUBLIC CONVENIENCE AND NECESSITY TO)
OWN AND OPERATE TRANSMISSION)
FACILITIES IN THE STATE OF ARKANSAS)
AND THE APPLICATION OF SOUTHWESTERN)
ELECTRIC POWER COMPANY TO TRANSFER)
CERTAIN SPECIFIED CECPN AUTHORITY AND)
RESPONSIBILITIES TO AEP SOUTHWESTERN)
TRANSMISSION COMPANY, INC.)**

DOCKET NO. 11-050-U

STAFF REPLY POST-HEARING BRIEF

Comes now the General Staff of the Arkansas Public Service Commission (Staff) and pursuant to Order No. 5 submits its Reply Post-Hearing Brief.

FEDERAL PREEMPTION

The Attorney General states that “this Commission is not required by federal law to accept FERC determined revenue requirements, returns on equity, capital structures, depreciation rates, or any other input used to set wholesale rate; this Commission need only defer to FERC rates or allocations within the wholesale electricity market.”¹ The AG’s purported distinction is the basis for his argument that the Commission may refuse to pass through the FERC jurisdictional SPP OATT charges paid by SWEPCO for transmission service because those charges are a “FERC revenue requirement”² instead of a FERC-established rate. The AG’s position makes a distinction where there

¹ AG Brief at 2.
² AG Brief at 14.

is no difference. FERC rates are based on FERC revenue requirements. In addition to appearing to be a mere case of semantics, the AG cites no support for this theory. As stated by the Court in *Nantahala Power and Light Company v. Thornburg*, 476 U.S. 953, 970 (1986), utilities must be able to recover “the costs incurred by their payment of just and reasonable FERC-set rates.” The FERC-set rate is the charge that SWEPCO pays for transmission service and is the basis for the expense which SWEPCO would be seeking to include in its rates. To the extent retail ratemaking policy does not provide for recovery of the FERC-based charges and instead sets a retail revenue requirement based on something other than that FERC rate, such conflicting state and federal regulatory policy can result in unrecoverable, or trapped costs.

The AG admits that “CURAD is unaware of any situation whereby an expense paid by a utility under the SPP OATT, which contains both costs and allocations, would not have to be passed through to retail ratepayers.”³ That is exactly what happens when SWEPCO pays SPP for transmission service under the SPP OATT. The AG’s attempt to label what SWEPCO pays as a “FERC revenue requirement” rather than a FERC rate and use that distinction as a basis for different treatment is simply in error. Transmission service is bought by SWEPCO from SPP under a FERC-established tariff. The AG never explains how this Commission can deny recovery of SWEPCO’s expenses which are incurred by paying a FERC-established rate.

The AG presents a “visual depiction of the status quo ... with SWEPCO as a member of the SPP”⁴ in order to provide background and explain “CURAD’s actual

³ AG Brief at 12.

⁴ AG Brief at 7.

position.”⁵ These over-simplified diagrams which purport to explain the difference between SWEPCO owning the transmission line and AEP Southwestern Transmission Company, Inc. (SW Transco) owning the same line are based on incorrect assumptions and are not accurate depictions of ratepayer impact. The AG focuses primarily on the flow of revenues and expenses in discussing alleged rate impacts purportedly based on “traditional” status quo ratemaking. The AG concludes that “[i]f the APSC decides those revenues do not matter for ratemaking purposes, or that SWEPCO should cover **all** costs of its transmission system using FERC revenue requirements, then no incremental harm to ratepayers would occur from its current application to establish a transco in Arkansas, because the Commission would have approved this rate increase anyway.”⁶ The flow of revenues and expenses matters for ratemaking purposes; however, all transmission revenues⁷ and expenses have already been considered by FERC in establishing a revenue requirement and the resulting OATT rates. Therefore this Commission is preempted from treating those revenues and expenses any differently than FERC has treated them in setting the FERC rates. This Commission is preempted from establishing transmission rates for either SWEPCO or SW Transco, because both entities are members of the SPP RTO and are subject to the FERC-approved SPP OATT. The diagrams presented by the AG simply are not appropriate for ratemaking purposes and are not meaningful where SWEPCO buys transmission service from SPP at the FERC-approved OATT rate.

⁵ AG Brief at 6.

⁶ AG Brief at 9-10 (emphasis in original).

⁷ Including transmission owner revenues.

An important point which the AG does not even acknowledge is the disparity between what retail ratepayers are paying SWEPCO for transmission service and what SWEPCO is in turn paying SPP. Using the simplified presentation of the Shipe Road line as illustrative of the revenue requirement, upon completion of the line, SWEPCO will incur \$745,996 in FERC OATT charges for use of the line if SWEPCO owns the line.⁸ Under current “traditional” retail ratemaking (with this Commission setting an Arkansas-specific revenue requirement for transmission which does not consider what SWEPCO pays in FERC OATT rates), Arkansas retail rates would be set to recover \$539,150, resulting in trapped costs of \$206,846.⁹ Under this example, this Commission avoids trapping costs if, in setting retail rates in the future, it instead uses the costs incurred by SWEPCO in paying the FERC-established rates. Staff notes that SWEPCO has not requested recovery of any differential between the transmission costs it recovers through its retail rates and any amounts it pays SPP pursuant to its FERC-approved OATT.¹⁰ Therefore, to the extent that there are any trapped costs currently, any such costs are the result of SWEPCO’s voluntary decision not to request recovery of those costs in retail rates.

The AG is only partially correct when he states, “If SWEPCO’s preferred transmission rider is approved, then retail ratepayers will have their rates for all

⁸ Or \$748,393 if SW Transco owns the line. See Bennett Direct Testimony at p. 16, Table 2, T. 227.

⁹ Or \$209,243 if SW Transco owns the line. The \$209,243 in trapped costs resulting from the difference between the SPP costs to provide transmission service incurred by SWEPCO and the revenues recovered from Arkansas through retail rates is the basis for the 38% rate impact that the AG has focused on in his case.

¹⁰ SWEPCO anticipates proposing a SPP-OATT transmission cost recovery rider in its next Arkansas base rate case to recover the SPP transmission cost incurred by SWEPCO to provide transmission service to Arkansas customers. See Bennett Direct Testimony at p. 14, T. 225.

transmission investment set using FERC revenue requirements.”¹¹ Because SWEPCO purchases transmission service from SPP at a FERC-approved rate, retail ratepayers will have their rates for all transmission investment set using that FERC-approved rate whether this Commission approves a transmission rider for SWEPCO or authorizes collection in base rates (or a combination of the two). As stated in Staff’s Initial Brief, it does not matter whether recovery is through a rider, base rates, or both. That decision can and should be made in SWEPCO’s next rate case. The only relevant point in this case rests on whether this Commission agrees that SWEPCO has the authority to recover the costs from FERC-established transmission rates that it pays to SPP.

The AG admits that “a state utility commission must allow, as reasonable operating expenses, costs incurred as a result of paying a FERC-determined wholesale rate”¹² and admits that expenses paid by a utility pursuant to the SPP OATT should be passed through to retail ratepayers¹³. However, the AG then asks this Commission to ignore some of the costs incurred by SWEPCO that it pays SPP for transmission service as a member of the RTO. The Commission cannot ignore those expenses that result from paying a FERC-established rate for transmission service. FERC has set an OATT rate which SWEPCO and other SPP transmission service buyers pay. This Commission cannot re-examine the FERC approved transmission rate, or its underlying components, to determine if it is reasonable or not. Furthermore, a *Pike County* exception to preemption is not appropriate here.¹⁴ SWEPCO cannot choose whether it buys transmission service from SPP. This Commission approved the transfer of

¹¹ AG Brief at 9 (emphasis in original).

¹² AG Brief at 11, quoting *Miss. Power v. Miss. ex rel. Moore*, 487 U.S. 354, 373 (1988).

¹³ AG Brief at 12.

¹⁴ *Pike Co. Light & Power Co. v. Penn. Pub. Serv. Comm’n*, 245 A.2d 735 (Pa. 1983).

operation of SWEPCO's transmission system to SPP in Docket No. 04-137-U. SWEPCO must take transmission service from SPP.

The AG states that this Commission will be "indirectly forced to use FERC revenue requirements (higher ROEs, unfavorable capital structures, etc.) in making retail rates" as a result of SW Transco owning the transmission line.¹⁵ It is not SW Transco's ownership of the transmission line but SWEPCO's membership in the SPP RTO, which requires it to pay SPP for transmission service at a FERC-approved rate, that is the basis for using FERC rates for ratemaking. FERC approves the appropriate SPP OATT rate based on the FERC revenue requirement no matter whether SWEPCO or SW Transco owns the line.

CONCLUSION

The AG provides no support for its theory that there is a distinction between FERC rates and revenue requirement with regard to ratemaking authority. Staff advocates setting retail rates by allowing, as a reasonable operating expense, transmission expenses incurred as a result of paying a FERC-determined wholesale price – the SPP OATT rate. The SPP OATT rate is based on the FERC-established transmission revenue requirement which includes all transmission revenues and expenses. It is unclear how this Commission could accept the "prices and quantities of FERC-approved wholesale sales in interstate commerce"¹⁶ in setting retail rates without "accept[ing] the FERC revenue requirement"¹⁷ upon which those prices are based.

¹⁵ AG Brief at 13.

¹⁶ AG Brief at 15.

¹⁷ *Id.*

The AG admits that if the Commission decides that SWEPCO should recover all its transmission expenses giving effect to the FERC-established rates, “then no incremental harm to ratepayers would occur from its current application to establish a transco in Arkansas.”¹⁸ Since retail ratemaking policy must allow recovery of the FERC-established transmission rates that SWEPCO pays, the retail ratemaking treatment for transmission costs would be the same whether SWEPCO owns the transmission line in question or the newly formed SW Transco owns the line. The ultimate retail transmission cost to ratepayers would be virtually the same. The evidence also shows that there is no downside to the proposal and that benefits to ratepayers are likely, in the form of lower costs to SWEPCO and SW Transco over time, which translate into lower transmission costs to ratepayers. Therefore, the application is in the public interest and should be granted.

Respectfully submitted,

General Staff of the Arkansas
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¹⁸ AG Brief at 10; see also at 15.

CERTIFICATE OF SERVICE

I, Valerie F. Boyce, hereby certify that a copy of the foregoing has been served on all parties of record by forwarding the same by electronic mail and/or first class mail, postage prepaid, this 9th day of April, 2012.

/s/ Valerie F. Boyce
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