UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Electric Transmission Incentives Policy Under Section 219 of the Federal Power Act	Docket No. RM20-10-000

REPLY COMMENTS OF WILLIAM TONG, ATTORNEY GENERAL FOR THE STATE OF CONNECTICUT, AND THE CONNECTICUT OIFFICE OF CONSUMER COUNSEL

Pursuant to the Federal Energy Regulatory Commission's ("FERC" or the " Commission") March 25, 2020 Notice of Proposed Rulemaking[1] ("NOPR") in the above-referenced proceeding, and the Supplemental Notice of Proposed Rulemaking (the "Supplemental NOPR") issued on April 15, 2021,[2] William Tong, Attorney General for the State of Connecticut and the Connecticut Office of Consumer Counsel provide the following reply comments.

INTRODUCTION

In the Supplemental NOPR, the Commission proposes to limit the duration of the grant of a 50 basis point Return on Equity ("ROE") incentive adder for participation by a transmission owner ("TO") in a Regional Transmission Organization ("RTO" and the "RTO Participation Incentive," respectively) to three years.[3] The Commission further

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[1] *Electric Transmission Incentives Policy Under Section 219 of the Federal Power Act*, 170 FERC ¶ 61,204 (2020).

[2] *Electric Transmission Incentives Policy Under Section 219 of the Federal Power Act*, Supplemental Notice of Proposed Rulemaking, 86 FR 21972 (Apr. 26, 2021), 175 FERC ¶ 61,035 (April 15, 2021).

[3] Congress authorized the Commission to approve transmission incentives as part of the Energy Policy Act of 2005 ("EPAct of 2005" adding section 219 to the Federal Power Act ("FPA"), codified at 16 USC §824s). The

proposes to require each utility that has already received an ROE incentive for joining and remaining in a transmission organization for three or more years to submit a compliance filing revising its tariff to remove the incentive from its transmission tariff.

DISCUSSION

In their comments to the Supplemental NOPR, the New England Transmission Owners ("NETOs") object to the Commission's proposal to limit the duration of the incentive adder to three years.[4] Specifically, the NETOs assert that: (i) FERC has the authority under Section 219(c) of the Federal Power Act ("FPA")[5] only to grant ROE transmission incentives, and not to amend or impose time limits on those incentives; (ii) FERC lacks authority to reduce or eliminate ROE transmission incentives without first making an affirmative finding that the existing ROEs (adding together the base ROE, with the various incentive ROE adders approved for a particular TO) are "unjust and unreasonable because exceeding the "zone of reasonableness" of ROEs;" and (iii) FERC lacks the authority under Section 219 to eliminate the 50 basis point incentive adder because the NETOs incentive adder was granted prior to and independent of FERC's

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Commission codified these transmission incentives in a rulemaking proceeding, *Promoting Transmission Investment through Pricing Reform*, Order No. 679, 116 FERC ¶ 61,057 (2006) ("Order 679"). The Commission, under its general, electric rate-making authority under Section 205 of the FPA, had approved individual non-cost-based transmission incentive adders prior to Section 219's effective date. *See, e.g.*, *Maine Public Utility Commission v. FERC*, 454 F. 3d 278 (D.C. Cir. 2006) (upholding FERC's initial grant of an incentive adder for the NETOs' membership in ISO-NE, operating as an RTO); *International Transmission Company v. FERC*, 988 F.3d 471 (D.C. Cir. 2021) (hereafter, *ITC*) (describing the ROE incentive adders granted by FERC to individual independent transmission companies prior to the enactment of Section 219 of the FPA).

[4] "Comments of the New England Transmission Owners in Opposition to the Elimination of the RTO Participation Incentive", dated June 24, 2021, in docket RM20-10 (referred to in the text as the "NETOs' Comments").

[5] 16 U.S.C. § 824s(c). The implementing regulation for the RTO Participation Incentive appears at 18 C.F.R. § 35.35(e); *Promoting Transmission Investment Through Pricing Reform*, Order No. 697, 116 FERC ¶ 61,057 (July 20, 2006) *order on reh'g*, Order No. 679-A, 117 FERC ¶ 61,345 (2006), *order on reh'g*, 119 FERC ¶ 61,062 (2007).

Order No. 679 (implementing the authority conferred by Section 219). All of these arguments are without merit.

1. FERC's authority to grant the RTO Participation Incentive includes the authority to limit its duration as proposed in the Supplemental NOPR.

The NETOs argue that, assuming Section 219 provides FERC the authority to award the RTO Participation Incentive in the first instance,[6] FERC has no authority to modify or revise the incentive once granted. This is a plain misreading of the statute. There was no directive nor inference in the Energy Policy Act of 2005 that such transmission incentives should be permanent or should never be subject to revision. To the contrary, the Act was clear that such incentives should be subject to review and revision.

Section 219 broadly authorizes FERC to establish "by rule" an "incentive-based" rate that includes among other matters, provision "for **incentives** to each transmitting utility or electric utility that joins a Transmission Organization." (Emphasis supplied). Section 219(d) further provides that "[a]ll rates approved under the rules adopted pursuant to this section [i.e., including the RTO Participation Incentive], **including any revisions to the rules**, are subject to the requirements of sections 824d and 824e of this title [FPA, Secs. 205 and 206], that all rate charges, terms and conditions be just and reasonable and not unduly discriminatory or preferential." (Emphasis added).

The statute uses the term "incentive," which necessarily is calibrated to induce a

[6] *See* discussion at Part 3, *infra*, addressing the NETOs' argument that Section 219 is not applicable to their circumstance in the first instance due to their taking membership in ISO-NE, configured as an RTO, and request for and receipt of an RTO Participation Incentive prior to the effective date of 18 C.F.R. § 35.35.

desired change in behavior. That is, there must be some "nexus" to achieving the change in behavior and not simply a "bonus."[7] The statute requires that any incentives granted under the rule are subject to the overall test of just and reasonable rates imposed by Sections 205 and 206 of the FPA. In Order 679 in its initial implementation of the statute, FERC explicitly applied the requirement of "nexus" (elaborating on the meaning of "incentive") to the RTO Participation Incentive by stating "we will approve, **when justified**, requests for public utilities that join and continue to be a member of an ISO, RTO or other Commission-approved Transmission Organization." (Emphasis added). Order 679, at P 326. Notably, the Commission also expressly reserved a decision on the duration of the incentive, stating, in relevant part: "We will not make a generic finding on the duration of incentives that will be permitted for public utilities that join Transmission Organizations." Order 679, at P 327. FERC's regulation, implementing the RTO Participation Incentive, essentially restates the statutory directive, requiring that it be "incentive-based" and requiring that recipients of the incentive first make a filing under Section 205 of the FPA and to "demonstrate" that the "proposed incentive-based rate

[7] In Order 679, implementing Section 219, FERC emphasizes the necessary linkage between the benefit granted and changed behavior by the beneficiary transmission owner, responding to the Congressional directive to provide for "incentives." FERC stated, in relevant part:

> It is true that our reforms adopted in the Final Rule [18 C.F.R. § 35.35] provide "incentives" to construct new transmission, but they do not constitute an "incentive" in the sense of a "bonus" for good behavior. … **each will be applied in a manner that is rationally tailored to the risks and challenges faced in constructing new transmission**. Not every incentive will be available for every new investment. **Rather, each applicant must demonstrate that there is a nexus between the incentive sought and the investment being made.** Our reforms therefore continue to meet the just and reasonable standard by achieving the proper balance between consumer and investor interests on the facts of a particular case and considering the fact that our traditional policies have not adequately encouraged the construction of new transmission.

Promoting Transmission Investment through Pricing Reform, Order No. 679, 116 FERC ¶ 61,057 at P 26 (2006)

treatment is just and reasonable and not unduly discriminatory or preferential."[8]

FERC therefore has the continuing obligation and authority to ensure that (a) there is sufficient nexus between the RTO Participation Incentive and an individual TO's behavior responding to the incentive, and (b) the incentive remains consistent with each TO's legally mandated "just and reasonable" overall level of rates. FERC also has the express statutory authority to revise the rule. Section 219(d). In the Supplemental NOPR, FERC is engaging in an inquiry to do precisely this by further evaluating, in light of changed circumstances, the appropriate duration of the RTO Participation Incentive and, depending on the results of its inquiry, to limit its duration. In this context, to conclude, as the NETOs urge, that FERC lacks statutory authority to adopt its proposal contained in the Supplemental NOPR distorts and misconstrues the statute.

2. FERC may properly terminate the duration of the RTO Participation Incentive in circumstances when the overall ROE recovered by a TO remains with the bounds of the "zone of reasonableness."

The NETOs further argue that FERC may not terminate the RTO Participation Incentive without first finding that the TOs' ROE (aggregating the TOs' base ROE and any incentive ROE adders, including the RTO Participation Incentive) exceeds the upper bound of the "zone of reasonableness" of ROEs. The NETOs rely upon the D.C. Circuit's ruling in *Emera Maine v. FERC*, 854 F.3d 9 (D.C. Cir. 2017) ("*Emera Maine*"), where the Court determined that in a complaint proceeding under section 206 of the FPA, FERC must first find that an existing base transmission rate is unjust and

[8] 18 C.F.R. § 35.55 (e).

unreasonable *before* establishing a new base transmission rate that it determines to be just and reasonable.

The NETOs are incorrect, and their reliance on *Emera Maine* is misplaced. First, the present rulemaking proceeding is not a complaint under Section 206 of the FPA, and there is no requirement that the Commission find that current transmission incentive policies are unjust or unreasonable before it amends or revises those policies. As noted above, Section 219(d) provides express statutory authority to revise the rules concerning transmission incentives. Indeed, to conclude otherwise would tend to undermine the very existence of transmission incentives, as there were no Commission findings that its then existing transmission incentive policy was unjust and unreasonable prior to its enactment of Section 219 in 2005 and the effective date of 18 C.F.R. § 35.35(c) in 2006.

Moreover, the NETOs' argument simply misconstrues the role of the incentive adders with respect to base ROE. The constitutional standards for assuring proper compensation to the TOs are secured by the base ROE.[9] The incentive adders, including the RTO Participation Incentive, are separate and legally distinct potential revenue sources paid to TOs, provided they are "justified" and have sufficient "nexus" to the desired result – the participation of the recipient TO in an RTO/ISO. The "zone of reasonableness" is relevant only as it is applied to **cap** the total ROE earned by a TO, adding together the base ROE and the cumulative level of incentive ROE adders. It is not

[9] *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679 (1923).

subsumed into a floor, so as to become a one-way ratchet used only to increase a TO's ROE.

FERC itself has clearly distinguished the differing functions of the two mechanisms; base ROE and the ROE incentive adders; in its recent decision in *Dayton Power and Light Company*, Order on Paper Hearing, 176 FERC ¶ 61,025 (July 15, 2021). In *Dayton*, the Commission focused on the issue of whether Dayton was entitled to the RTO Incentive Payment if the utility's participation in an RTO was already mandated by Ohio law, so that the proposed incentive would therefore not effect any change in behavior in the utility, because already compelled by applicable state law. In denying the grant of a RTO Participation Incentive to *Dayton*, the Commission distinguished ROE incentive adders from the base ROE, stating:

> Dayton also argues that the Commission should grant Dayton the RTO Adder because not doing so threatens Dayton's financial integrity, credit ratings, and/or ability to attract investment. Dayton's argument is misplaced. One of the requirements of a utility's base ROE, as established in *FPC v. Hope Natural Gas Co.* and *Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm'n of W. Va.*, is to preserve the utility's financial integrity and enable the utility to attract capital investment. **Therefore, it is the base ROE, rather than incentives such as RTO Adder, that was intended to ensure a utility's financial integrity**. In contrast, as the Commission stated in Order No. 679, the basis for the RTO Adder is a recognition of the benefits that flow from membership in RTOs/ISOs and to incentivize utilities to join them. Therefore, **the Commission's decision to deny the incentive RTO Adder here is irrelevant to Dayton's base ROE and financial integrity, credit ratings, and ability to attract investment**. (Footnotes omitted)(emphasis added).

Id., P 29.

The NETOs' conflation of base ROE and incentive adders here is similarly misplaced. The NETOs' base ROE for regional electric network transmission plant, the subject of a long-running series of FERC rulings and court appeals,[10] is distinct from the

[10] *See, e.g.*, *Emera Maine*, 854 F.3d 9, 24 (D.C. Cir. 2017).

RTO Participation Incentive. FERC has the authority to limit the RTO Participation Incentive as proposed in the Supplemental NOPR, notwithstanding that the overall ROE earned by a TO is less than the upper boundary of its ROE "zone of reasonableness." Moreover, FERC has preserved the procedural protections and allocation of burden of proof for implementing the proposed duration restriction on the RTO Participation Incentive by requiring a tariff filing, subject to review under Section 206 of the FPA, reflecting the removal of the RTO Participation Incentive from the TO's rates. Supplemental NOPR at P 11.

3. The NETOs Pre-FERC Rule approval of an RTO Participation Incentive does not Bar FERC from Applying any Limit on the Duration of the RTO Participation Incentive to them.

The NETOs argue that they became members of ISO-NE as part of an arrangement that included the grant of a 50 basis point ROE incentive award filed for and approved prior to the effective date of the FERC regulation implementing Section 219(c) of the FPA. The NETOs therefore argue that their incentive award is not subject to the requirements of the regulation, now or as it might be revised by FERC pursuant to the Supplemental NOPR.[11] The NETOs further argue that the transmission incentive was adopted as part of a broader settlement arrangement converting ISO-NE into a RTO. In this regard, the incentive adder was bargained for in consideration of other concessions, and should FERC eliminate it, the NETOs might reconsider their participation in ISO-

[11] The NETOs put it bluntly both as to the regulation and Commission action under the Supplemental NOPR. Per the NETOs: "Order No. 679 has no bearing on the incentive granted to the NETOs." NETOs' Comments at 2. "[T]he proposed change in this proceeding [referring to the Supplemental NOPR] to modify the Commission's regulations implementing FPA section 219 cannot apply to NETOs' rates." *Id*. at 25.

NE. These arguments are also without merit.

On February 19, 2021, the D.C. Circuit upheld a decision by the Commission cutting transmission incentives previously granted to three electric transmission companies. In *International Transmission Company v. FERC*, 988 F3d. 471 (D.C. Cir. 2021) ("*ITC*"), the Court reviewed a parallel section of 18 C.F.R. § 35.55 addressing ROE incentives awarded to three independent transmission companies. These transmission companies, International Transmission Company ("ITC"), Michigan Electric Transmission Company ("METC"), and ITC Midwest, LLC ("Midwest"), like the NETOs, had received ROE incentive adders granted by FERC prior to the effective date of the rule in 2006.

As the Court noted, the 2006 rule was a "codification" of the ROE incentive adders and followed a pre-existing practice of the Commission (as is true of the RTO Participation Adders also codified into the Commission's rule). As the court stated:

> The 2006 rule [18 C.F.R. § 35.55 (b)(1), (d)(2)] was the first codification of that incentive [for participation in an independent transmission company or Transco, but also for the RTO Participation Incentive, codified at the same time in the same rule in § 35.35(e)], but it reflected a preexisting FERC practice of granting independent and standalone transmission companies "adders" to their base return on equity [including for RTO Participation as in the case of the NETOs]. As its name suggests, a FERC authorized return on equity determines the extent to which a utility in the highly regulated electricity sector may earn a profit. FERC ties "adders" to certain behaviors or characteristics of utilities, incentivizing needed actions by bumping up their returns on equity above the base level set by FERC. The first "Transco adders" were granted in 2003 to *International Transmission Company* (ITC) and *Michigan Electric Transmission Company* (METC), two of the petitioners in this case. *ITC Holdings Corp.*, 102 FERC ¶ 61,182 (2003); *METC*, 105 FERC ¶ 61,214 (2003); *see also METC*, 113 FERC ¶ 61,343 (2005).

ITC, 988 F3d. at 474. The NETOs provide an extensive discussion of the history of their RTO Participation Incentive from: (1) its genesis in a filing with FERC in 2003 arising with their agreement to membership in a reconfigured ISO-NE; (2) the initial approval of

the filing by FERC in 2004, each pre-dating the enactment of Section 219 in 2005 and the effective date of 18 C.F.R. § 35.35(c) in 2006, and; (3) through the decisions by the courts on appeal of FERC's approvals. The NETOs, however, offer no basis for distinguishing their circumstances from those of ITC and METC and the Court decision reviewing FERC's ROE incentive adder, based on FERC's incentive adder regulation, as applied to those companies. Like the NETOs, ITC and METC followed early FERC transmission ROE incentive policies, pre-dating 18 C.F.R. § 35.35, in crafting their case-specific ROE incentive adder awards. Like the NETOs, the transmission companies' adders were approved by FERC prior to the rule's effective date and coupled with contractual and governance re-organizations, "voluntarily" contracted for by the entities forming ITC and METC. FERC's pre-existing authority to approve incentive adders for ITC, METC and the NETOs was similarly codified and confirmed by Section 219 of the FPA and implemented through 18 C.F.R. § 35.35. The Commission plainly has the authority under Section 219 to revise, amend or eliminate transmission incentives.[12]

Finally, the Commission should reject the implied threat that the NETOs present should the FERC eliminate the transmission incentives. The NETOs argue that their participation in ISO-NE and continuing agreement to ISO-NE's operational control of

[12] The court decision, upholding on appeal the initial grant by FERC of the NETOs' RTO Participation Incentive (*Maine PUC v. FERC*, *supra*), is to similar effect, finding the initial grant to the NETOs, pre-dating Section 219, to fall permissibly within the scope of the exercise of FERC's general rate-making authority under the FPA (454 F.3d at 287) and subsumed within the express authority granted to FERC regarding transmission ROE incentives created by Section 219, "even if the adder power now falls within FERC's authority," while remaining also subject to FERC's general rate-making authority conferred by Sections 205 and 206 (454 F. 3d at 289). Section 219 re-enforces this conclusion in that it expressly provides for the continuing application of the Commission's general rate-making jurisdiction over incentives granted under the statute's implementing regulation. Section 219(d).

and planning responsibility for regional transmission is "voluntary," and can be undone should the Commission reduce their transmission incentive. A number of the NETOs, however, have independent commitments to cede operational control of their facilities to ISO-NE. After the reconfiguration of ISO-NE as an RTO, several of the NETOs effected large mergers/acquisitions (*e.g.*, Northeast Utilities and NSTAR ("the NU Merger"), Central Maine Power and United Illuminating (the "Avangrid Merger"), Central Vermont Public Service and Green Mountain Power, collectively comprising 85% of the net plant comprising the regional network electric transmission grid within ISO-NE's operating footprint).[13] These mergers were reviewed and approved by the Commission, all occurring in a manner in which the merging companies "voluntarily" agreed to the

[13] *See Comments of American Manufacturers* (July 1, 2020) ("*AM Comments*") in FERC docket No. RM20-10-000, exhibit AMF-5.

regulatory conditions to their acquisitions/mergers.[14] [15] [16] During the regulatory review of each of these mergers, these NETOs made key representations that the merged companies could not exercise vertical market power because control, administration and planning of the regional transmission grid and generating facility interconnections was the responsibility of ISO-NE, consistent with its functioning as an RTO and **not** the merging companies. These representations were expressly cited in FERC's approval of the mergers, conditioning the inquiry undertaken by the Commission in arriving at its

[14] *NSTAR, Northeast Utilities*, Docket No. EC11-35, 136 FERC ¶61,016 (July 6, 2011), Para. 53 ("Applicants explain that Northeast Utilities and NSTAR have turned over control of their transmission facilities to ISO-NE and cannot exercise vertical market power by controlling transmission.") Para. 56 ("We [FERC] find that Applicants' ownership of electric transmission facilities does not raise any vertical market power concerns because Applicants have turned over control of their facilities to ISO-NE, eliminating their ability to use its transmission system to harm competition."); NSTAR et al., Northeast Utilities et al., *Application under Secs. 203(a)(1) and 203 (a)(2) of the Federal Power Act for Authorization of Disposition of Jurisdictional Assets and Merger* (Jan. 7, 2011), pp. 23-24. ("The transmission facilities of the Applicants are under the operational control of ISO-NE, which is a Commission-approved RTO. The Transaction therefore does not provide the Applicants the ability to abuse their ownership or control of transmission facilities to give themselves an advantage in energy markets… Furthermore, ISO-NE, not the Applicants, controls the interconnection process for new generation facilities. [footnotes omitted].")

[15] *Iberdrola, UIL Holding Corporation, Order Authorizing Disposition of Facilities*, 151 FERC ¶62,148 (June 2, 2015) ("All of Applicants' transmission assets are under the control of ISO-NE or NYISO… Applicants conclude that the Proposed Transaction creates no vertical market power concerns."). *Joint Application for Authorization of Transaction under Section 203 of the Federal Power Act and Requests for Waivers of Filing Requirements*, Shortened Comment Period and Expedited Consideration (March 25, 2015), p. 6 ("As described in the attached Hieronymus Affidavit, the extent of Applicants' business transactions in the same geographic market is de minimis. None of the Iberdrola Applicants own or control transmission assets other than the transmission assets in New York and Main that are operated by NYISO and ISO-NE, respectively, and those limited facilities necessary to interconnect their generating facilities to the transmission grid. UIL does not own or control transmission assets other than the transmission assets in Connecticut that are operated by ISO-NE and those limited facilities necessary to interconnect their generating facilities to the transmission grid. Dr. Hieronymus concludes that there are no vertical market power issues arising from the Applicants' ownership of transmission assets because all of the Applicants' transmission assets are under the control of either ISO-NE or NYISO.")

[16] *CVPSCo. et al*., 138 FERC ¶ 61,161 (2012). "[T]he Commission has found that turning over operational control of transmission facilities to an independent entity eliminates any concerns about transmission-related vertical market power because it eliminates the ability for the merged firm to use its transmission system to harm competition in wholesale electricity markets. Here, Applicants have turned over control of their transmission facilities to ISO-NE. Therefore, we do not need to reach the issue of whether the merged firm will have control over VELCO and find that there is no need to impose vertical market power mitigation." *Id.*, P 37.

decision to issue the approvals. *Id.* These NETOs commitments to RTO membership were not a wholly "voluntary" act that can now be undone in their own discretion. The NETOs have made commitments to the Commission to cede operational control of their facilities to ISO-NE consistent with the public interest.

Finally, the NETOs' threat to dissolve ISO-NE as an RTO is wholly disproportionate to the revenues involved. The 50 basis point ROE incentive collectively paid to the NETOs is approximately $36 million (2020) annually.[17] This is less than 5% of the approximately $1B in total return on equity recovered annually by the NETOs for their regional electric transmission assets from New England electric ratepayers. The NETOs should more properly be focused on the substantial investment opportunities the regional operators will be planning in the future as the New England economy, and particularly the electric sector, transitions toward a Net Zero Carbon Emissions world.

[17] *See Comments of American Manufacturers* (July 1, 2020) in FERC docket No. RM20-10-000, p. 25 ($72 million (2019) estimated annual revenue for each 100 basis point change to the ROE on regional network electric transmission plant for electric transmission owners in ISO-NE). Eversource disclosed in its First Quarter, 2021, 10Q SEC report (at p. 45) that it estimates the potential annual company-specific reduction in earnings from the termination of the 50 bps ROE incentive to be $14 million (after-tax). The regional network electric transmission rate base of Eversource and its affiliates is approximately 58% of the total regional network transmission rate base. *See AM Comments*, Exhibit AMF-5. Based on this information (and assuming a similar equity/total capital structure across the other NETOs), the pre-tax annual effect of the termination of the ROE incentive adder would be approximately $30.4 million (2019).

Respectfully Submitted,

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CERTIFICATE OF SERVICE

I, John Wright, hereby certify that on this day I caused the foregoing to be served upon all parties identified on this agency's service list for this proceeding.

Dated: July 26, 2021