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UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

	)	
Constellation Mystic Power, LLC	)	Docket No. ER18-1639
	)	

INITIAL BRIEF OF THE ATTORNEY GENERAL OF MASSACHUSETTS

PROTECTED MATERIAL REDACTED

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20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

TABLE OF CONTENTS

Procedural Background 1
Argument 5
I. Whether the rate proposed to be collected under the Mystic Cost-of-Service Agreement ("Mystic Agreement") is just and reasonable?..............................5
A. Whether the proposed calculation of non-fuel costs is just and reasonable?...
i. Whether the proposed annual fixed revenue requirement ("AFRR") for Mystic 8 & 9 is just and reasonable?...5
1. Whether the proposed rate base for Mystic 8 & 9 are just and reasonable? 5
a. Are the proposed gross and net plant values used in the proposed AFRR just and reasonable? 5
b. Is the proposed accumulated depreciation just and reasonable?..13
c. Whether there should be a reduction in rate base for regulatory liability to reflect excess deferred income taxes? 13
d. Is the proposed cash working capital ("CWC") just and reasonable? 13
2. Whether the proposed weighted average cost of capital for Mystic 8 & 9 is just and reasonable 13
a. Whether the proposed return on equity is just and reasonable?..14
i. Is the proposed proxy group just and reasonable?......................15
ii. Are the growth rates used to calculate the implied cost of equity for the proposed AFRR appropriately calculated? 19
iii. Is the proposed placement of Mystic's return on equity within the range of DCF results just and reasonable?..............20
b. Whether the proposed capital structure is just and reasonable? 23
c. Whether the proposed cost of debt is just and reasonable?..............24
B. Whether the proposed fuel costs are just and reasonable? 25
i. Whether the proposed Fixed O&M/Return on Investment component of the Monthly Fuel Supply Cost is just and reasonable?..25
1. Is the proposed rate base for Everett just and reasonable? 25
a. Are the proposed gross and net plant values used for Everett just and reasonable? 25
b. Is the proposed accumulated depreciation just and reasonable?...31
c. Is the proposed cash working capital ("CWC") just and reasonable? 31
2. Whether the proposed rate of return on equity for

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

Everett is just and reasonable? 31
a. Should Everett's return on equity have a different placement than Mystic within the range of DCF results? 32
ii. Whether the proposal to include all costs of Everett as Mystic fuel costs, less an appropriate credit for third party sales of LNG, is just and reasonable and what constitutes an appropriate revenue credit? 32
1. Whether the Fuel Supply Agreement, winter penalties and planning to procure gas for the coldest winter in 50 years create incentives to over-schedule LNG and artificially depress natural gas prices? 37
2. Whether the Fuel Supply Agreement will create an improper subsidy by ratepayers for third-party natural gas sales? 38
3. Whether the costs of owning and operating the Everett Marine Terminal should be allocated between those incurred to service Mystic, on the one hand, and those incurred for third party sales, on the other hand, for purposes of determining cost recovery under the proposed Mystic Cost of Service Agreement? 38
4. Whether (i) the proposed percentages of profit to which Constellation LNG and Mystic would be entitled with respect to third-party sales of gas has been justified and (ii) the calculation of any profit sharing incentive for third party sales of gas should be performed *ex post* rather than *ex ante*? 38
5. Whether ISO-NE should be required to engage a third-party expert to assess the prudence of Mystic's and Constellation's gas procurement and management decisions, and following such assessments, file any disallowances with the Commission under Section 205? 39
iii. Whether the remaining components of the Monthly Fuel Supply Costs are just and reasonable? 39
iv. Whether the remaining terms and conditions of the Amended and Restated Fuel Supply Agreement ("FSA") result in rates under the Mystic Agreement that are just and reasonable? 39
C. Whether the proposed Schedule 3A is just and reasonable, and satisfies the Commission's directive to develop a true-up? 39
i. Whether the proposed true-up information exchange process and challenge protocols are just and reasonable? 40
D. Whether a claw back provision should be adopted, and if so, what amounts should be refunded and under what circumstances/conditions? 40
II. Whether the terms and Conditions of the Mystic Agreement have been shown to be just and reasonable, and not unduly discriminatory? 42

A. Whether the Constellation LNG-Constellation Mystic Power LLC Fuel Supply Agreement will enable affiliate abuse or have anticompetitive effects in relevant natural gas and electricity markets? 42
III. Whether there are other aspects of the proposed rate to be collected under the Mystic Agreement that are not just and reasonable, and whether additional terms and conditions of the Mystic Agreement, or additional transactional rules should be adopted? 42
Conclusion 43

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

TABLE OF AUTHORITIES

Cases

Atlantic Refining Co. v. Pub. Serv. Comm'n, 360 U.S. 378 (1959) 2, 4, 7
Bluefield Waterworks and Improvement Co. v. Public Serv. Comm'n of West Virginia, 262 U.S. 679 (1923) 14, 15
California Oregon Power Co. v. FPC, 150 F.2d 25 (9th Cir. 1945) 12
Emera Maine v. FERC, 854 F.3d 9 (D.C. Cir. 2017) 20
Fed. Power Comm'n v. Hope Natural Gas Co., 320 U.S. 591 (1944) 14
Montana Power Co. v. FERC, 559 F.2d 295 (9th Cir. 1979) 11
Pa. Elec. Co. v. FERC, 11 F.3d 207 (D.C. Cir. 1993) 33
S. Cal Edison Co. v. FERC, 717 F.3d 177 (D.C. Cir. 2013) 20
Southern California Edison Company, 717 F.3d 177 (D.C. Cir. 2013) 15
Union Electric Co. v. FERC, 890 F.2d 1193 (D.C. Cir. 1989) 34

Agency Decisions

Ass'n of Bus. Advocating Tariff Equity, 156 FERC ¶ 61, 234 (2016) 15
Atlantic Path 15, LLC, 133 FERC ¶ 61,153 (2010). 15
Bangor Hydro-Electric Co., et al., 122 FERC ¶ 61,038 (2008) 7
Bangor Hydro-Electric Co., et al., 122 FERC ¶ 61,038 (2008) 4
Cove Point LNG, LLC, 68 FERC ¶ 61,128 (1994) 26
Distrigas Corp., 47 F.P.C. 752 (1972) 26, 29
Distrigas of Massachusetts, LLC, 124 FERC ¶61,039 (2008) 26, 29, 30
Enbridge Pipelines (KPC), 100 FERC ¶61,260, at P 173 (2002) 24
Enbridge Pipelines (KPC), 109 FERC ¶61,042 (2004) 30
Entergy Services, Inc., 156 FERC ¶61,196 (2016) 1, 12
Goldendale Energy Center, LLC and Puget Sound Energy Inc., 118 FERC ¶62,101 (2007) 6
Indiana & Michigan Power Company, 4 FERC ¶61,316, (1978) 23
ISO New England, 161 FERC ¶ 61,031 (2017) 21
Locust Ridge Gas Co., 29 FERC ¶61,052 (1984) 2, 6, 25
Longhorn Partners Pipeline, 73 FERC ¶61,355 at 62,112-62,113 (1995) 30
Louisiana Gas Co., 7 FERC ¶61,316 (1979) 29, 30
Martha Coakley et al. v. Bangor Hydro-Electric Co. et al., 165 FERC ¶ 61,030 (2018) 14, 16, 20, 21
Mid-Louisiana Gas Co, 7 FERC ¶61,316 at 61,684 (1979). 30
Midwest Independent System Operator, Inc., 116 FERC ¶63,030 (2006) 3, 32
Midwest Independent System Operator, Inc., 141 FERC ¶ 63,021 (2012) 2, 4, 7
Minnesota Power & Light Co., 43 FERC ¶61,104 (1988) 7

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

N. States Power Co., 64 FERC ¶61,324 (1993). 33
New York Independent System Operator, Inc., 155 FERC ¶61,076 (2016).......... 41
New York Independent System Operator, Inc., 161 FERC ¶61,189 (2017).......... 41
Northern Gas Co., 35 FERC ¶61,114 (1986).......... 29, 30
PacifiCorp, 124 FERC ¶61,046 (2008) .... passim
Portland Natural Gas Transmission System, 142 FERC ¶61,197 (2013) 22
Potomac-Appalachian Transmission Highline, LLC, 158 FERC ¶61,050 (2017) 15
PSEG Lawrenceburg Energy Company LLC, American Electric Power Service Corporation, AEP Generating Company, 119 FERC ¶61,015 (2007).......... 6
Quachita Power, LLC and Entergy Arkansas, Inc., 122 FERC ¶62,071 (2008). 6
S. Cal Edison Co., 131 FERC ¶61,020 (2010).......... 20
Seaway Crude Pipeline Co., LLC, 154 FERC ¶61,070 (2016) 7, 28
See Minnesota Power & Light Co., 43 FERC ¶61,104 (1988) 2
South Carolina Generating Company, Inc., 40 FERC ¶61,116 (1987) 23
Southern California Edison Co., 131 FERC ¶61,020 (2010).......... 15
Trailblazer Pipeline Co., 106 FERC ¶63,005 (2004) 24
Transcontinental Gas Pipe Line Corp, 80 FERC ¶61,157 (1997) 23
Transcontinental Gas Pipeline Co., 80 FERC ¶ 61,157 (1997) 3

Statutes

18 C.F.R. § 385.704.......... 1
18 C.F.R. § 385.706.......... 1

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Constellation Mystic Power, LLC	)))	Docket No. ER18-1639

INITIAL BRIEF OF THE ATTORNEY GENERAL OF MASSACHUSETTS

The Attorney General of the Commonwealth of Massachusetts ("Massachusetts Attorney General") submits her Initial Brief pursuant to Rules 704 through 706 of the Commission's Rules of Practice and Procedure[1] and the Commission's July 13, 2018 Order Accepting and Suspending Filing and Establishing Hearing Procedures.[2]

INTRODUCTION AND SUMMARY

In this proceeding Constellation Mystic Power LLC ("Mystic") seeks Commission approval of a Cost of Service Agreement between itself and ISO New England ("ISO-NE") which would establish the rates New England ratepayers will pay to keep Mystic 8 & 9 in commercial operation for a two year period (June 1, 2022 to May 31, 2024). Mystic bears the burden of establishing that the rates it proposes are just and reasonable.[3] It has failed to satisfy this burden.

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[1] 18 C.F.R. §§ 385.704-385.706.
[2] *Constellation Mystic Power, LLC*, 164 FERC ¶61,022 at P 12 (2018).
[3] *Entergy Services, Inc.*, 156 FERC ¶61,196 at P 17 (2016) ("The allocation of the burden of proof in a Section 205 proceeding is 'well-established' with the public utility bearing the burden to justify a rate increase.")

Instead, the Cost of Service Agreement contravenes well established Commission precedents designed to implement the Federal Power Act's purpose of "afford[ing] consumers a complete, permanent and effective bond of protection from excessive rates and charges."[4] As discussed further below, Mystic's proposal results in unjust and unreasonable rates for numerous reasons.

First, in developing its proposed gross and net plant values for Mystic 8 & 9, and the Everette Marine Terminal ("Everett"), Mystic ignores the Commission's requirement that a utility may record only the lesser of the depreciated original cost or actual purchase price of an asset.[5] The original cost principle is designed to protect ratepayers from being subjected to "widespread abuses" resulting from utilities selling assets at ever increasing prices which would otherwise result in ever increasing rates for the same level of benefits.[6] The history of these units illustrates precisely the concerns that animate the original cost principle. The Commission should reject Mystic's attempt to evade this precedent.

Second, Mystic's proposed weighted average cost of capital ("WACC") reflects an excessive return on equity ("ROE") and inappropriately imputes Exelon Generating's ("ExGen") equity heavy capital structure and cost of debt. Mystic's proposed 10.71 percent ROE is the median of the upper half of range of reasonableness produced by an upwardly biased proxy group which fails to follow

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[4] *Midwest Independent System Operator, Inc.*, 141 FERC ¶ 63,021 at P 525 (2012), *citing Atlantic Refining Co. v. Pub. Serv. Comm'n*, 360 U.S. 378, 288 (1959).

[5] *Locust Ridge Gas Co.*, 29 FERC ¶61,052 at 61,114 (1984).

[6] *PacifiCorp*, 124 FERC ¶61,046 at P28 (2008). *See Minnesota Power & Light Co.*, 43 FERC ¶61,104 at 61,342, *order on reh'g*, 43 FERC ¶61,502, *order on reconsideration*, 44 FERC ¶61,302 (1988).

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

Commission precedent. Proper application of Commission precedent produces a ROE of no higher than 8.22 percent.

Mystic's proposal to impute ExGen's 67.28 percent equity/32.72 percent debt capital structure is similarly misplaced. The Commission has recognized that its "ratemaking policies provide an incentive" for corporate parents "to create and maintain an equity rich capital structure" as a way of maximizing profits.[7] Given the anomalously equity heavy nature of ExGen's capital structure, the more appropriate capital structure to impute is Exelon Corporation's more balanced capital structure of 48.13 percent equity/ 51.87 percent debt.

Third, Mystic's request to recover 100 percent of Everett's fixed and variable costs, subject to a 50 percent margin sharing on forward sales, is an egregious example of Mystic's overreaching in this proceeding and fundamentally violates the cost causation principle, which is "one of the bedrocks of cost allocation and rate design principles."[8] The record shows that Mystic 8 & 9 can use no more than 39.16 percent of Everett's output. Permitting Mystic to recover the costs of Everett in this manner would distort several crucial market signals and remove the incentives for Mystic to operate Everett in an efficient and economic manner, thereby harming regional fuel security and the New England wholesale electric market. Given that this entire proceeding is premised on the need to retain Mystic 8 & 9 for fuel security purposes, it makes no sense to allow a cost of service structure that has the potential to distort the allegedly fragile New England natural gas market. To

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[7] *Transcontinental Gas Pipeline Co.*, 80 FERC ¶ 61,157, 61,664 (1997).
[8] *Midwest Independent System Operator, Inc.*, 116 FERC ¶63,030 at P 227 (2006).

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

properly reflect cost causation principles and protect the region's markets, the Commission should allocate no more than 39.16 percent of Everett's fixed and variable costs to New England ratepayers for the duration of the Cost of Service Agreement.

Mystic's proposal presents issues of first impression and therefore has the potential to set dangerous precedent which could lead to a cascade of similar cost of service filings in New England. As a result, the Commission should carefully scrutinize each element of Mystic's request to ensure the integrity of the long standing ratemaking principles that allow the Commission to carry out its "mandate to ensure that rates are neither less than compensatory to the seller nor excessive to the consumer."[9] For the reasons discussed in more detail below, the Commission should find that Mystic's proposal would result in rates that are unjust and unreasonable and reject the filing. Any acceptance of the filing should be narrowly tailored to the conditions presented in this proceeding and should be conditioned on a compliance filing requiring Mystic to address the concerns identified below.

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[9] *Bangor Hydro-Electric Co., et al.,* 122 FERC ¶ 61,038 at P 14 (2008). *See also Midwest Indep. Transmission Sys. Operator*, 141 FERC ¶ 63,021 at P 525 (2012) ("the Court has stated that the FPA 'was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges.") (*citing Atlantic Refining Co. v. Pub. Serv. Comm'n*, 360 U.S. 378, 288 (1959)).

PROCEDURAL BACKGROUND

The Massachusetts Attorney General adopts and incorporates the Parties' October 11, 218 Joint Procedural History.[10]

ARGUMENT

In accordance with Commission practice and the Proposed Joint Statement of Issues ordered by Judge Sterner to guide this proceeding, the Massachusetts Attorney General's Initial Brief adopts the structure adopted by the parties' September 19, 2018 Proposed Joint Statement of Issues in order to ease the Commission's review and ensure consistency with the briefs of other parties.

I. Whether the rate proposed to be collected under the Mystic Cost-of-Service Agreement ("Mystic Agreement") is just and reasonable?

A. Whether the proposed calculation of non-fuel costs is just and reasonable?

i. Whether the proposed annual fixed revenue requirement ("AFRR") for Mystic 8 & 9 is just and reasonable?

1. Whether the proposed rate base for Mystic 8 & 9 is just and reasonable?

a. Are the proposed gross and net plant values used in the proposed AFRR just and reasonable?

[10] The Massachusetts Attorney General has focused on the issues most relevant to its concerns in this proceeding. Failure to address a specific issue should not be interpreted as support for Mystic's position on that issue.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

No, Mystic's proposed gross and net plant values do not reflect the lower of original cost or Exelon's actual purchase price, and therefore are not just and reasonable. The Commission's "long standing policy on property acquisitions is to allow a purchaser to record acquisitions at the lesser of (i) the depreciated original cost or (ii) the actual purchase price."[11] The Commission's original cost principle requires that "amounts included in the accounts for electric plant acquired as an operating unit or system to be stated at the cost incurred by the person who first devoted the property to utility service."[12] The original cost principle applies to merchant generating facilities seeking cost of service rates because those facilities are considered devoted to public service when they make sales "pursuant to a Commission approved market-based rate tariff."[13]

The original cost principle plays a critical role in ensuring that rates remain just and reasonable. As the Commission has explained:

> The Commission's original cost principle is a long-standing accounting policy adopted in response to widespread abuses in the electric utility industry that arose through the practice of selling properties at large profits to other public utilities followed by the acquiring utilities' inflating plant accounts (and rate base) by the premium paid. The result of this practice was that ratepayers paid higher rates for electric service but received no increase in benefits. Under the original cost principle, amounts paid in excess of depreciated original cost are recorded as an

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11 *Locust Ridge Gas Co.*, 29 FERC ¶61,052 at 61,114 (1984).

12 *PacifiCorp*, 124 FERC ¶61,046 at P 27 (2008).

13 *Id.* at P 31. *See also Goldendale Energy Center, LLC and Puget Sound Energy Inc.,* 118 FERC ¶62,101 (2007); *PSEG Lawrenceburg Energy Company LLC, American Electric Power Service Corporation, AEP Generating Company*, 119 FERC ¶61,015 (2007); *Quachita Power, LLC and Entergy Arkansas, Inc.*, 122 FERC ¶62,071 (2008).

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

> acquisition adjustment…and amortized below-the-line as a shareholder expense.[14]

Put another way, "[w]ithout the original cost concept 'all that need be done to raise rates and obtain greater income would be to have one company buy utility properties from another at higher prices than depreciated original cost and in this very simple way increase the cost of service to consumers."[15] Mystic's own witness Dr. Olson similarly testified:

> If we go back more than a hundred years, there was a great dispute under public utility regulation about how value should be determined, and value is of course the rate base and it's multiplied by rate of return, and the common practice at that time was to attempt to add to the value of rate base by using fair value adjustments, inflation, reproduction costs, a variety of ways. And original cost was the concept that regulators came up when the Uniform System of Accounts was developed so as to essentially freeze the recovery of, and the return on, rate base to the original cost, and that's why the definition includes the first person to own the property, so the markups are not permitted.[16]

As a result, the original cost principal is an essential tool for the Commission in carrying out its "mandate to ensure that rates are neither less than compensatory to the seller nor excessive to the consumer."[17]

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14 *PacifiCorp*, 124 FERC ¶61,046 at P28. *See Minnesota Power & Light Co.*, 43 FERC ¶61,104 at 61,342, *order on reh'g*, 43 FERC ¶61,502, *order on reconsideration*, 44 FERC ¶61,302 (1988).

15 *Seaway Crude Pipeline Co., LLC*, 154 FERC ¶61,070 at P 90 (2016).

16 Tr. 445:22-446:9 (Olson)

17 *Bangor Hydro-Electric Co., et al.,* 122 FERC ¶ 61,038 at P 14 (2008). *See also Midwest Indep. Transmission Sys. Operator*, 141 FERC ¶ 63,021 at P 525 (2012) ("the Court has stated that the FPA 'was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges.") (*citing Atlantic Refining Co. v. Pub. Serv. Comm'n*, 360 U.S. 378, 288 (1959)).

Here, despite this precedent, the gross and net plant values Mystic proposes to include in its cost of service for Mystic 8 & 9 do not reflect either Exelon's acquisition cost or the depreciated original cost for the units, making it impossible to apply the Commission's requirements. Mr. Heintz testified that he calculated his gross and net plant values based on **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]** This difference is critical here, and is at the heart of why Mystic's proposed gross and net plant values for Mystic 8 & 9 are unjust and unreasonable. A little history of these units, which have changed ownership six times since their development,[20] is necessary to illuminate this point:

The units were developed by Sithe Energies, Inc. and entered commercial operation in mid 2003 after being acquired by Exelon Boston Generation, an Exelon subsidiary.[21] A few months later, Exelon decided to "transition out of ownership"[22] of Mystic 8 & 9, likely in response to pressure it was feeling from EBG Holdings, its lenders. In the process, Exelon took a $573 million impairment against Mystic 8 &

[21] ENC-0032 at 2-3.
[22] ENC-0032 at 3.

9,[23] which **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]**. By early 2004 Exelon had reached a deal to avoid foreclosure and transferred Mystic 8 & 9 (along with other assets) to Boston Generating LLC, a special purpose entity owned by EBG Holdings.[24]

In 2007, EBG Holdings merged with another entity to form US Power Generating Company, which **[BEGIN CUI/PRIV-HC]**

[END CUI/PRIV-HC]

In early 2011, Constellation Energy Group, Inc. ("Constellation") purchased Mystic Units 7, 8, and 9, Mystic Jet, and Fore River generating Units from US Power Generating Co. for $1.1 billion.[29] **[BEGIN CUI/PRIV-HC]**

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[23] *Id.*, *citing* Exelon SEC Form 8-K, filed October 23, 2003; Exelon SEC Form 10-Q filed October 29, 2003 at 35-36).

[24] ENC-0032 at 3.

[29] ENC-0032 at 5.

[END CUI/PRIV-HC]

In 2012, Exelon reacquired Mystic 8 & 9 following a merger with Constellation. **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]**

As the history above shows, the value of the Mystic 8 & 9 units has changed drastically as these units have changed owners. To highlight just one example, Constellation paid approximately $1.1 billion in 2011 for a total of five assets (Mystic 7, 8, 9, Fore River and Mystic Jet), yet in this proceeding Mystic proposes a gross plant figure of just over $1 billion for just Mystic 8 & 9[34] despite the fact that Exelon sold Fore River to Calpine Corp. for $530 million.[35] The history of these assets illustrates precisely the kind of "fair value adjustments" and "variety of

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34 MYS-0009.

35 Calpine Corp. Form 10-K for Fiscal Year Ending December 31, 2014 at 47.

ways" to increase rate base that so concerned the Commission and caused it to adopt the original cost principle in the first place.[36] Permitting Mystic to recover cost of service rates based on its proposed gross and net plant values would result in "ratepayers pa[ying] higher rates for electric service but receiv[ing] no increase in benefits"[37] and would therefore be unjust and unreasonable.

Mystic's proposed gross and net plant values for Mystic 8 & 9 **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]** However the Court of Appeals has upheld the original cost principle in the face of similar "hardships." In *Montana Power Co. v. FERC,* the Court of Appeals for the Ninth Circuit upheld the application of the original cost rule when a utility paid $3,250,000 for a transmission line whose depreciated original cost was only $156,117.[40] The Court recognized that:

> Because the market value of assets seldom changes precisely in accordance with depreciation, depreciated original cost is often not an accurate proxy of current fair market value. Nonetheless, original cost accounting is employed to avoid the difficulties of more subjective methods of property valuation. The original cost method has been

[36] Tr. 445:22-446:9 (Olson).
[37] *PacifiCorp*. 124 FERC ¶61,046 at P 28.
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[40] *Montana Power Co. v. FERC*, 559 F.2d 295 at 296-298 (9th Cir. 1979).

> applied to property acquisitions by utilities to prevent utilities from artificially inflating their rate bases by acquiring properties at unrealistically high prices. … Reviewing courts have consistently upheld the application of the original cost rule to property acquisitions by utilities. … The purpose of the FPC accounting regulations, we observed, 'was … to eliminate the padding from utility accounts. The provision has the broad purpose of protecting the public against artificially inflated investment costs on the basis of which utility companies assert the right to a return.'[41]

While it is clear that the original cost principle must be applied to determine the appropriate gross and net plant values, the record in this proceeding does not include sufficient information to identify the depreciated original cost for Mystic 8 & 9. Mystic has therefore failed to meet its Section 205 burden[42] and the Commission should reject Mystic's filing with leave for Mystic to refile. In the alternative, the Commission should require Mystic to make a compliance filing to propose, and properly support, gross and net plant values which reflect the lower of Exelon's acquisition cost or depreciated original cost. Given the complexity of calculating gross and net plant values, Mystic should be required to produce all relevant and necessary supporting data for party review as part of any compliance filing.

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[41] *Id.* at 300, *quoting California Oregon Power Co. v. FPC*, 150 F.2d 25 at 28 (9th Cir. 1945).

[42] *Entergy Services, Inc.*, 156 FERC ¶61,196 at P 17 (2016) ("The allocation of the burden of proof in a Section 205 proceeding is 'well established' with the public utility bearing the burden to justify a rate increase.")

b. Is the proposed accumulated depreciation just and reasonable?

The Massachusetts Attorney General supports the position of Eastern New England Consumer-Owned Systems ("ENECOS") on this issue.[43]

c. Whether there should be a reduction in rate base for regulatory liability to reflect excess deferred income taxes ("EDIT").

The Massachusetts Attorney General supports the position of Commission Trial Staff witness Latone on this issue. The Massachusetts Attorney General supports the inclusion of a regulatory liability of $44,451,330 as a reduction to rate base as well as the remainder of Ms. Latone's recommendations.[44]

d. Is the proposed cash working capital ("CWC") just and reasonable?

The Massachusetts Attorney General supports the position of New England States Committee on Electricity ("NESCOE") witness Cannady on this issue. The Massachusetts Attorney General supports setting the CWC for Mystic 8 & 9 at $0 and disallowing a fuel lag allowance for the reasons articulated in Ms. Cannady's testimony.[45]

2. Whether the proposed weighted average cost of capital for Mystic 8 & 9 is just and reasonable?

No. Mystic's proposed WACC for Mystic 8 & 9 reflects an excessive 10.71 percent ROE and incorrectly imputes ExGen's anomalously equity heavy capital structure and cost of debt. The proposed WACC is therefore unjust and

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[43] Ex. ENC-0030 REVISED at 64:18-66:10; Exhibit ENC-0042; ENC-0047.
[44] Ex. S-0018 at 14:5-12.
[45] NES-010 at 5:15-9:21.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

unreasonable. The correct WACC must reflect an 8.22 percent ROE and Exelon Corporation's capital structure of 48.13 percent equity and 51.87 percent debt, and 4.09 percent cost of debt.

a. Whether the proposed return on equity is just and reasonable?

Mystic's proposed 10.71 percent ROE for Mystic 8 & 9 is excessive, calculated in violation of well settled Commission precedent, and is therefore unjust and unreasonable.[46] The Commission should set the ROE for Mystic 8 & 9 at no higher than 8.22 percent, which is the median of a properly conducted discounted cash flow ("DCF") analysis.

A just and reasonable ROE must be "commensurate with returns on investment in other enterprises having corresponding risks" and should be no higher than what is "sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain [a utility's] credit and to attract capital."[47] When identifying a just and reasonable ROE for a single utility, like Mystic, Commission

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[46] The Massachusetts Attorney General recognizes that the Commission issued an order in Docket No. EL11-66 on October 16, 2018 announcing a change to its ROE methodology. *Martha Coakley et al. v. Bangor Hydro-Electric Co. et al.*, 165 FERC ¶ 61,030 (2018). The record here, which closed prior to that order's issuance, lacks the evidentiary basis to apply that new precedent, so the Massachusetts Attorney General briefs this issue addressing only the DCF methodology.

[47] *Fed. Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944); *see also Bluefield Waterworks and Improvement Co. v. Public Serv. Comm'n of West Virginia*, 262 U.S. 679, 692 (1923) ("The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties.")

precedent uses the median of a two-step discounted cash flow ("DCF") method.[48] As discussed in more detail below, Mystic's proposal to set the ROE at 10.71 percent, which is the median of the upper half of an upwardly biased proxy group, violates the tenants of *Hope* and *Bluefield*, Commission precedent, and is unjust and unreasonable.

i. Is the proposed proxy group just and reasonable?

No, Mystic's proposed proxy group is a results driven exercise that fails to apply well established Commission precedent and therefore does not produce a proxy group of utilities with risks comparable to Mystic. Comparable risk is a pivotal determination in identifying a just and reasonable ROE because a utility "has no constitutional right to profits such as are realized or anticipated in highly profitable or speculative ventures."[49] In recognition of this fact, the Commission has held that the primary concern in selecting a proxy group is identifying "companies with comparable risks to those facing the applicant"[50] and has adopted a series of screens to ensure the resulting proxy group is of comparable risk to the target utility. As a result, a properly conducted proxy group will include only those utilities who:

(1) are considered electric utilities by Value Line;

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48 *Potomac-Appalachian Transmission Highline, LLC*, Opinion No. 554, 158 FERC ¶61,050 (2017) (use of two-step DCF methodology); *Ass'n of Bus. Advocating Tariff Equity*, Opinion No. 551, 156 FERC ¶ 61, 234 (2016) (use of two-step DCF methodology); *Southern California Edison Company*, 717 F.3d 177, 181-182 (D.C. Cir. 2013) (use if median of the zone of reasonableness); *Southern California Edison Co.*, 131 FERC ¶61,020 at PP 84-95 (2010).

49 *Bluefield*, 262 U.S. at 692-693.

50 *Atlantic Path 15, LLC*, 133 FERC ¶ 61,153 at P 13 (2010).

(2) have a credit rating no more than one notch above or below the utility whose ROE is at issue;

(3) pay dividends and have neither made more announced a dividend cut during the applicable six month study period;

(4) have no merger activity during the six month study period that is significant enough to distort study inputs; and

(5) whose ROE results pass thresholds tests of economic logic, including both a low-end outlier test and a high-end outlier test.[51]

Staff witness Mr. Keyton's proxy group appropriately applies these screens and identifies a proxy group containing twelve utilities which produces a range of reasonableness of 6.81 percent to 10.54 percent.[52]

By contrast, Mystic witness Dr. Olson's proxy group contains only seven utilities and produces a significantly higher range of reasonableness of 9.24 percent to 11.87 percent. Dr. Olson achieves this upward bias by inventing new proxy group screens and ignoring existing ones.

First, Dr. Olson applies a "revenue" screen to eliminate any potential proxy group member with less than $2 billion in revenue.[53] The application of this screen has a dramatic effect on the resulting proxy group and removes seven proxy group members who would otherwise be included.[54] The revenue screen targets those proxy group members who would form the lower end of a properly constructed proxy group. For illustration, when applied to Mr. Keyton's properly constructed proxy

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[51] *Martha Coakley, et al., v. Bangor Hydro-Electric Co. et al.*, 165 FERC ¶61,030 at P 49 (2018).

[52] Ex. S-0010 at 3.

[53] Ex. MYS-0010 at 13:16-18.

[54] Ex. CT-001 at 23:16-18.

group, the $2 billion revenue screen eliminates the five lowest members of his twelve member proxy group.[55]

The Commission has never applied a $2 billion revenue screen and Dr. Olson has produced no evidence to support the screen other than his own personal judgment.[56] Tellingly, the record indicates Dr. Olson himself has not used this revenue screen in other cases before the Commission,[57] making its application here a transparent attempt to increase the resulting ROE. The Commission should reject such a results driven deviation from Commission policy.

Second, Dr. Olson ignores the Commission's merger and acquisition activity screen by including Dominion Energy, Sempra, and Avangrid in his proxy group despite record evidence of merger activity significant enough to distort DCF inputs. Dominion Energy announced its plans to acquire SCANA in a $7.9 billion transaction on January 2, 2018.[58] The following day, January 3, 2018, Dominion's share price dropped 3.85%. This change was the single largest percentage change in daily share price over the period August 1, 2017 to July 31, 2017, and was five and a half times larger than the average price change of 0.73 percent.[59] As a result, the record illustrates that Dominion's ongoing attempts to acquire SCANA were

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55 Ex. CT-001 at 23:16-18; Ex. S-0011 at 3 (Removal of IDACORP (6.81 percent); NorthWestern Corp. (7.17 percent); Black Hills Corp. (7.48 percent); El Paso Electric (7.55 percent); and PNM Resources (7.73 percent). The revenue screen would additionally eliminate OGE Energy Corp. (8.66) and Otter Tail Corp. (10.54)).

56 Ex. S-0011 at 3.

57 ENC-0001 at 22:3-7.

58 Ex. S-0013 at 176.

59 ENC-0001 at 14:3-7.

significant enough to distort one of the DCF inputs which requires its exclusion from the proxy group.

Sempra was involved in two different merger related transactions during the applicable study period in this proceeding, and therefore must be excluded from the proxy group. First, Sempra concluded its acquisition of Oncor in March of 2018, which falls within the study period for this proceeding.[60] Second, Sempra's price surged by as much as 18 percent following press reports that investors viewed the company as undervalued.[61] Sempra's stock price prior to this announcement was $101.43 per share, which rose to $119.78 per share on the day of the announcement.[62] The investor presentation that spurred this price surge recommended that Sempra sell assets, and on June 28, 2018 Sempra announced its intention to sell multiple assets including its entire portfolio of U.S. wind and solar assets.[63] These transactions had a clear impact on Sempra's stock price, and therefore were significant enough to require exclusion.

The stock price for Avangrid, which sets the high end of Dr. Olson's proxy group, rose 34 percent in 2017, making it one of the top performing utilities for that year.[64] Value Line attributed this unusual stock boost to "takeover speculation."[65] Avangrid's stock price has continued to rise since that Value Line report, making it clear that investors' expectation of an acquisition have distorted the stock price, one

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60 ENC-0001 at 57:14-16.
61 S-0009 at 3:19-23.
62 *Id.* at 31:23-32:2.
63 *Id.* at 32:6-15.
64 Ex. S-0013 at 98.
65 Ex. S-0010 at 25:21-26:2.

of the DCF inputs.[66] Further, Avangrid's unique position as a controlled company means that its financial structure is so fundamentally different from either Mystic or the other members of the proxy group that it cannot be considered to face comparable risk to Mystic.[67] Iberdrola S.A. owns 81.5% of Avangrid's stock, meaning any remaining shareholders are in such a minority position that they have no ability to impact corporate decision making.[68] Witnesses for Commission Staff, ENECOS and the Connecticut Department of Energy and Environmental Protection, and the Connecticut Office of Consumer Counsel ("CT Parties") all agree that Avangrid's position as a controlled company means it faces risks that fundamentally differ from those of Mystic or any of the other proxy group members, and therefore must be excluded from any proxy group. For the reasons discussed above, Dr. Olson's proposed proxy group deviates from Commission precedent, and therefore cannot be used to identify a just and reasonable ROE.

ii. Are the growth rates used to calculate the implied cost of equity for the proposed AFRR appropriately calculated?

No, Mystic witness Dr. Olson's DCF analysis includes incorrectly calculated long-term growth rates which renders all of Dr. Olson's growth rates incorrect. The

[66] ENC-0001 at 27:8-13.
[67] ENC-0001 at 24:1-27:6.
[68] ENC-0001 at 24:11-16.

Massachusetts Attorney General supports the positions of ENECOS,[69] Commission Staff,[70] and the CT Parties on this issue.[71]

iii. Is the proposed placement of Mystic's return on equity within the range of DCF results just and reasonable?

No, Mystic's proposal to place the ROE at the median of the upper half of the zone of reasonableness violates Commission precedent, is unsupported, and produces an ROE that is unjust and unreasonable. The Commission uses the median of a properly constructed proxy group to identify a just and reasonable ROE for a single utility like Mystic.[72] Here, the median of Mr. Keyton's proxy group is 8.22 percent.

Mystic's arguments in support of straying from the Commission's precedential preference for the median are unpersuasive. First, Mystic witness Olson asserts the median of the upper half of the zone is necessary because current capital market conditions are anomalous.[73] Dr. Olson relies on Opinions No. 531 and 551 to support his upward adjustment despite the fact that Opinion No. 531 has been vacated and remanded by the United States Court of Appeals for the District of Columbia Circuit.[74] The Commission has explicitly held that Opinion No.

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[69] ENC-0001 at 28:1-31:3.

[70] S-0009 at 34-38.

[71] CT-0001 through CT-0009.

[72] *Martha Coakley et al. v. Bangor-Hydro Electric Co. et al.*, 165 FERC ¶61,030 at P 17 note 46 (2018); *S. Cal Edison Co.*, 131 FERC ¶61,020 at P 91 (2010), *remanded on other grounds sub. nom. S. Cal Edison Co. v. FERC*, 717 F.3d 177, 183-87 (D.C. Cir. 2013).

[73] MYS-0010 18:23-19:1

[74] *Emera Maine v. FERC*, 854 F.3d 9 at 27 (D.C. Cir. 2017).

531 "cannot serve as precedent in other proceedings."[75] Dr. Olson's upward adjustment should be dismissed on this ground alone. However, even if Dr. Olson could properly rely on prior Commission orders on this issue, he has failed to put forward sufficient evidence on the topic to carry the heavy burden of justifying his proposed upward adjustment.[76] Additionally, while witnesses in other ROE proceedings have dedicated "a substantial portion of their evidentiary presentations"[77] to the question of whether anomalous conditions exist and whether they distort the DCF, Dr. Olson has dedicated less than six pages between both his direct and rebuttal testimony to establishing the existence of anomalous capital market conditions.[78] Such scant discussion falls far short of carrying the burden of establishing that market conditions are sufficiently "anomalous" to warrant an upward adjustment of the ROE.

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75 *ISO New England*, 161 FERC ¶ 61,031 at P 28 (2017) ("we recognize that, as a result of the Court's vacatur, those opinions [531] cannot serve as precedent in other proceedings. That effect is significant. For example, in 2016, the Commission issued Opinion No. 551…In making its determinations in that proceeding, the Commission relied extensively on its conclusions in Opinion No. 531. Rehearing of Opinion No. 551 is now pending before the Commission. As a result of *Emera Maine*, the Commission will not be able to rely on Opinion No. 531 as precedent in addressing those rehearing requests.")

76 *Martha Coakley et al. v. Bangor Hydro-Electric Co. et al.*, Opinion No. 531-B, 150 FERC ¶ 61,165 at 62,155 (Commissioner Honorable concurring) ("Any public utility that seeks to rely upon anomalous market conditions to justify placement of its base ROE in the upper end of the zone of reasonableness will be tasked with demonstrating, in each case, that market conditions are indeed anomalous and that the adequacy of a base ROE set at the midpoint of the zone of reasonableness should be scrutinized. The utility should expect a rigorous analysis of the record when it attempts to make such a demonstration.")

77 *Martha Coakley et al. v. Bangor Hydro-Electric Co. et al*, 165 FERC ¶61,030 at P 43.

78 MYS-0029 at 7:19-8:3, 10:14-20, 12:14-16 MYS-0029 at 7:19-8:3, 10:11-20, 12:10-16.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

Second, Dr. Olson asserts that Mystic faces risks greater than the other members of his proposed proxy group.[79] The Commission does consider the risk profile of the target entity as it compares to the members of the proxy group itself. However, as discussed above, Dr. Olson's proxy group fails to follow Commission precedent and produces a proxy group of utilities who are not risk comparable to Mystic. Therefore, discussions of whether Mystic faces risks greater than the members of Dr. Olson's proxy group are moot.

Additionally, Dr. Olson's argument fails even if the Commission were to adopt his proxy group. The Commission presumes an entity to be of average risk and has held that "unless [an entity] makes a very persuasive case in support of the need for an adjustment and the level of the adjustment proposed, the Commission will set the [entity's] return at the median of the range of reasonable returns."[80] Dr. Olson's discussion of this topic is little more than his unsupported statement that "merchant generation is more risky than a combination of integrated electric utility operations."[81] As a threshold matter, whether merchant generation is more risky is irrelevant to this proceeding which involves determining the just and reasonable ROE for a cost of service agreement. But even setting that issue aside, Dr. Olson's fleeting testimony on the issue clearly fails to make the "very persuasive case"

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[79] MYS-0010 at 19:1-5.

[80] *Portland Natural Gas Transmission System*, 142 FERC ¶61,197 at P 382 (2013) (Commission presumes a pipeline to be of average risk "absent highly unusual circumstances that indicate an anomalously high or low risk as compared to other pipelines. Thus, unless a pipeline makes a very persuasive case in support of the need for an adjustment and the level of the adjustment proposed, the Commission will set the pipeline's return at the median of the range of reasonable returns.").

[81] MYS-0029 at 6:10-11.

necessary to support an adjustment to the upper half. In fact, given that the ROE at issue will apply during a cost of service period, Mystic's risk is *lower* as compared to the proxy group, not higher.[82] As a result Dr. Olson's attempts to argue Mystic faces higher levels of risk than proxy group members stands in direct contradiction to the Commission's repeated recognition of the risk reducing nature of cost of service rates.[83] Mystic's proposal to place the ROE for Mystic 8 & 9 in the upper half of the zone of reasonableness should therefore be rejected.

b. Whether the proposed capital structure is just and reasonable?

No, Mystic's proposal to use impute ExGen's 67.28 percent equity/32.72 percent debt capital structure to Mystic is unjust and unreasonable. The appropriate capital structure to impute is Exelon's, which as of December 31, 2017 was 48.13 percent equity/51.87 percent long-term debt.[84] While it prefers to use actual capital structures, Commission precedent permits imputing a capital structure to entities like Mystic who do not issue their own debt or have their own credit rating.[85] When imputing a capital structure, the Commission examines whether the parent's capital structure "is anomalous relative to the capital

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[82] ENC-0001 at 66:9-11.

[83] *South Carolina Generating Company, Inc.*, 40 FERC ¶61,116, 61,311 (1987); *Indiana & Michigan Power Company*, 4 FERC ¶61,316, 61,739 (1978).

[84] CT-001 at 6:14-7:8.

[85] *Transcontinental Gas Pipe Line Corp.*, Opinion No. 414, 80 FERC ¶61,157 at 61,667 (1997).

structures of the publicly-traded proxy companies used in the DCF analysis" and whether use of the capital structure will produce a just and reasonable rate.[86]

Here, ExGen's 67.28 percent equity/32.72 percent debt is anomalous relative to the capital structures of the utilities contained in Mr. Keyton's proxy group. The members of Mr. Keyton's proxy group have equity ratios ranging from 32.40 percent to 58.70 percent, with an average of 48.19 percent and a median or 49.30 percent.[87] As a result, ExGen's capital structure is clearly anomalous as compared with the members of the proxy group companies being used in the DCF analysis to identify a just and reasonable ROE. The Massachusetts Attorney General supports the use of Exelon's capital structure for the reasons articulated by Commission Staff[88] and the CT Parties.[89]

c. Whether the proposed cost of debt is just and reasonable?

Mystic's proposal to use ExGen's cost of debt is unjust and unreasonable. Exelon's 4.09 percent cost of debt is just and reasonable for the reasons articulated by the witnesses on behalf of Commission Staff[90] and the CT Parties.[91]

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[86] *Enbridge Pipelines (KPC)*, 100 FERC ¶61,260, at P 173 (2002) ("The Commission's policy is to use the actual capital structure of the entity that does the financing for the regulated pipeline as long as it results in just and reasonable rates."); *Trailblazer Pipeline Co.*, 106 FERC ¶63,005 at P 68 (2004) (Holding Commission policy permits use of corporate parent's capital structure provided the use does not create anomalous results in reliance on witness testimony which imputed the ultimate parent's capital structure to the pipeline).

[87] S-0009 at 48:14-20.

[88] S-0009 at 44:4-52:8.

[89] CT-001 at 17:14-20:13.

[90] Ex. S-0009 at 52:13-15; S-0011 at 4-5.

[91] Ex. CT-001 at 20:15-17.

B. Whether the proposed fuel costs are just and reasonable?

i. Whether the proposed Fixed O&M/Return on Investment component of the Monthly Fuel Supply Cost is just and reasonable?

1. Is the proposed rate base for Everett just and reasonable?

a. Are the proposed gross and net plant values used for Everett just and reasonable?

Similar to its approach for Mystic 8 & 9, Mystic's proposed gross and net plant values for Everett do not reflect the lower of original cost or Exelon's actual purchase price, and therefore are not just and reasonable. As discussed in more detail in Section I.A.i.1.a above, the Commission's "long standing policy on property acquisitions is to allow a purchaser to record acquisitions at the lesser of (i) the depreciated original cost or (ii) the actual purchase price."[92] The original cost principle requires that "amounts included in the accounts for electric plant acquired as an operating unit or system to be stated at the cost incurred by the person who first devoted the property to utility service"[93] and a facility is considered dedicated to public service when it makes sales pursuant to a Commission approved tariff.[94]

Here, **[BEGIN CUI/PRIV-HC]** [redacted]

[redacted]

[redacted] **[END CUI/PRIV-HC]** Distrigas of Massachusetts, LLC's

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92 *Locust Ridge Gas Co.*, 29 FERC ¶61,052 at 61,114 (1984).
93 *PacifiCorp*, 124 FERC ¶61,046 at P 27 (2008).
94 *PacifiCorp*, 124 FERC ¶61,046 at P 27 (2008).
[redacted] [redacted]

("DOMAC") dedicated Everett to public service in 1971,[96] and its books are therefore relevant for determining Everett's depreciated original cost. **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]** must be recognized as a reduction to Everett's original cost.

Determining Exelon's actual purchase price for Everett is not straight forward, but is clearly **[BEGIN CUI/PRIV-HC]**

96 *Distrigas Corp.*, 47 F.P.C. 752 (1972); *Distrigas of Massachusetts, LLC*, 124 FERC ¶61,039 (2008)

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

[END CUI/PRIV-HC]

Mystic argues **[BEGIN CUI/PRIV-HC]**

[END CUI/PRIV-HC] Under the substantial benefits test, to include a purchase price above depreciated original cost in rate base a utility must:

> First, . . . show that the facilities will be converted from one public use to a different public use, or that the assets will be placed in FERC-jurisdictional service for the first time. Second, the [utility] must show clear and convincing evidence that its acquisition of the facilities will provide substantial, quantifiable benefits to ratepayers even if the full purchase price, including the portion above depreciated original cost is included in rate base. The Commission also considers whether the transaction at issue is an arm's length sale between unaffiliated parties, and whether the purchase price of the asset at issue is less than the cost of constructing a comparable facility. The Commission allows an acquisition premium to be included in a [utility's] rate base when the purchase price is less than the cost of constructing comparable facilities, the facility is converted to a new use, and the transacting parties are unaffiliated.[108]

[108] *Seaway Crude Pipeline Co. LLC*, 154 FERC ¶61,070 at P 92 (2016).

The substantial benefits test represents an exception to the original cost principle and the Commission has recognized that the utility seeking to prove substantial benefits has a "heavy burden that may be 'practically impossible' to meet."[109]

Mystic's acquisition of Everett fails the first prong because the purchase in no way changes Everett's existing public use. Everett was first dedicated to public service in 1971[110] and the Mystic units in 2003.[111] Mystic 8 & 9 have been reliant on Everett as their sole source of LNG since their development[112] and until recently that relationship has existed contractually with Everett and Mystic under separate ownership structures. Mystic's arguments that the Cost of Service Agreement somehow changes the nature of Everett's public use are unpersuasive and contradicted by the record. First, Mystic's argument that Everett's role in providing fuel security constitutes a differing public use is incorrect. Prior to the cost of service period Everett will be the sole source of LNG to Mystic 8 & 9 and will provide LNG sales to third parties pursuant to the contractual arrangements in place between Mystic, Everett, and any applicable third party. This situation will continue during the cost of service period, and the fact that the terms of those contracts or the parties with whom Everett contracts may differ is not sufficient to constitute a different public use. Exelon's acquisition does not change the product

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109 *Northern Gas Co.*, 35 FERC ¶61,114, 61, 236 (1986), *quoting Louisiana Gas Co.*, 7 FERC ¶61,316, 61,684 (1979).

110 *Distrigas Corp.*, 47 F.P.C. 752 (1972); *Distrigas of Massachusetts, LLC*, 124 FERC ¶61,039 (2008)

111 ENC-0032 at 2-3.

112 Mystic Transmittal Letter at 2.

Everett provides or the market it serves, and therefore it fails the first prong.[113] Mystic's argument that the Cost of Service Agreement will bring Everett under Commission rate jurisdiction ignores the fact that Everett was subject to the Commission's jurisdiction from 1971 until when it abandoned its NGA Section 7 certificate in 2003.[114] As a result, Mystic has failed to carry its heavy burden to satisfy the first prong of the test.

Mystic fairs no better under the second prong, under which Mystic bears the "heavy burden"[115] of providing clear and convincing evidence that its acquisition of Everett will provide substantial and quantifiable benefits to ratepayers. These benefits "must be tangible and non-speculative and must be quantifiable in monetary terms."[116] Mystic provides virtually no analysis of these alleged benefits aside from an assertion that acquiring Everett is cheaper than the alternatives.[117] This falls far short of a burden the Commission notes can be "practically impossible to meet"[118] and which requires monetary quantification of any asserted benefits. For the reasons discussed above, **[BEGIN CUI/PRIV-HC]**

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113 *Enbridge Pipelines (KPC)*, 109 FERC ¶61,042 at P 27 (2004) (referencing a change from the provision of crude oil to natural gas as a different public use); *Longhorn Partners Pipeline*, 73 FERC ¶61,355 at 62,112-62,113(1995) (finding a different public use when pipeline changed from transporting crude oil to refined products, reversed its flow and upgraded the line itself which allowed service "of a new market distinct from the market…previously served").

114 *Distrigas of Massachusetts LLC*, 124 FERC ¶61,039 at PP 4, 6, 7.

115 *Northern Gas Co.*, 35 FERC ¶61,114, 61, 236 (1986), *quoting Louisiana Gas Co.*, 7 FERC ¶61,316, 61,684 (1979).

116 *Mid-Louisiana Gas Co*, 7 FERC ¶61,316 at 61,684 (1979).

117 *See e.g.* MYS-0001 at 6, 11-14; MYS-0020 at 12-13.

118 *Northern Gas Co.*, 35 FERC ¶61,114, 61, 236 (1986), *quoting Louisiana Gas Co.*, 7 FERC ¶61,316, 61,684 (1979).

[END CUI/PRIV-HC] should be rejected.

b. Is the proposed accumulated depreciation just and reasonable?

No, the proposed accumulation and depreciation fails to incorporate past impairment charges and is therefore unjust and unreasonable. The Massachusetts Attorney General supports the position of ENECOS[119] and NESCOE[120] on this issue.

c. Is the proposed cash working capital ("CWC") just and reasonable?

No, the proposed CWC is not just and reasonable. The Massachusetts Attorney General supports the position of NESCOE witness Cannady on this issue.[121]

2. Whether the proposed rate of return on equity for Everett is just and reasonable?

No, Mystic's proposed 10.71 percent ROE for Everett is unjust and unreasonable for the reasons addressed in Section I.A.i.2.a.iii above. Everett should receive an ROE no higher than 8.22 percent. Further, as discussed below, should the Commission accept Mystic's proposal to allocate 100 percent of Everett's fixed and variable costs to Mystic 8 & 9, the ROE for Everett should be placed at or near the low end of Mr. Keyton's range of reasonableness.

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[119] ENC-0030 REVISED at 64:18-66:10; ENC-0042; ENC-0047.
[120] NES-021, NES-024, NES-025.
[121] NES-010.

a. Should Everett's return on equity have a different placement than Mystic within the range of DCF results?

Mystic proposes to allocate 100 percent of Everett's fixed and variable costs to Mystic 8 & 9. The Commission should reject this request for the reasons discussed in Section B.2.a.ii below. However, should the Commission decide to adopt Mystic's proposal, the ROE for Everett should be placed at or near the bottom of Mr. Keyton's range of reasonableness. A lower placement for Everett's ROE would be required because allocating 100 percent of Everett's fixed and variable costs to Mystic 8 & 9 would substantially reduce the risk Everett faces, and it would therefore no longer be appropriate to place Everett's ROE at the median of the range of reasonableness.

ii. Whether the proposal to include all costs of Everett as Mystic fuel costs, less an appropriate credit for third party sales of LNG, is just and reasonable; and what constitutes an appropriate revenue credit?

Mystic proposes to allocate 100 percent of Everett's fixed and variable costs, subject to a 50 percent margin on forward sales, to Mystic 8 & 9 despite the fact that those units can use no more than 39.16 percent of Everett's capacity. [122] Mystic's proposal violates the cost causation principle, "one of the bedrocks of cost allocation and rate design principles" [123] which requires that customers "should be charged rates that fairly track the costs for which they are responsible."[124] "The

[122] NES-028 at 26:22-27:2.
[123] *Midwest Independent System Operator, Inc.*, 116 FERC ¶63,030 at P 227 (2006).
[124] *Pa. Elec. Co. v. FERC*, 11 F.3d 207, 211 (D.C. Cir. 1993).

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

fundamental theory of Commission ratemaking is that cost should be recovered in the rates of those customers who utilize the facilities and thus cause the costs to be incurred."[125] Here, the simple fact is that supplying 100 percent of Mystic 8 & 9's needs requires only 39.16 percent of Everett's capacity.[126] Accepting Mystic's proposal would require customers to pay rates as if they are utilizing 100 percent of Everett. New England ratepayers should not be forced to finance 100 percent of the costs of a facility from which they can receive only 39.16 percent of the benefits. Any other allocation would result in New England ratepayers inappropriately subsidizing Everett. The Commission should therefore permit no more than 39.16 percent of Everett's fixed and variable costs to be allocated to Mystic 8 & 9.

Additionally, allocating 100 percent of Everett's costs to Mystic 8 & 9 removes the incentive to efficiently and prudently operate Everett in a manner that benefits the region and minimizes ratepayer costs.[127] The Court of Appeals has noted: "The matching of rates with costs contributes to the efficient use of the service. … As Professor Khan has noted, 'the only economic function of price is to influence *behavior*."[128] Accepting Mystic's proposal removes the price signals and market

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[125] *N. States Power Co.*, 64 FERC ¶61,324, 63,379 (1993). *See also Pa. Elec. Co. v. FERC*, 11 F.3d 207, 211 (D.C. Cir. 1993) ("utility customers should normally be charged rates that fairly track the costs for which they are responsible").

[126] NES-028 at 26:22-27:2.

[127] CT-010 at 7:10-8:18.

[128] *Union Electric Co. v. FERC*, 890 F.2d 1193, 1198 (D.C. Cir. 1989), *citing* Alfred E. Khan, *Application of Economics to Utility Rate Structures* Public Utilities Fortnightly, Jan. 19, 1978 at 13, 15. Cf. James C. Bonbright, Albert L Danielsen, and David R. Kamerschen, *Principles of Public Utility Rates* 95-101 (3 ed. 1988)).

functions that are necessary to ensure that the Everett facility is used in a way that minimizes costs while maximizing regional benefits.

ISO-NE's recognition of this defect motivated its decision to request the retention of 50 percent of the margin on all forward sales in an effort to artificially recreate the market incentives eliminated by Mystic's cost allocation proposal. However, this number, which is unsupported by any analysis or experience,[129] only partially restores the incentives achieved through proper cost allocation and would require significant modification as explained in detail in the testimony of the witnesses for NESCOE and the CT parties.[130] As a result, the Commission should require Mystic to follow standard cost allocation principles instead of trying to artificially recreate these incentives through a margin sharing mechanism.

Ignoring cost causation principles raises concerns beyond just the inefficient use of the Everett facility. Allocating all of Everett's costs to Mystic 8 & 9 insulates Everett from any market related risk by creating a ratepayer subsidy,[131] which in turn creates the potential for anticompetitive behavior which could harm the New England natural gas market and in turn the wholesale energy market.[132] This is an unacceptable outcome, especially in a proceeding allegedly motivated by the need to protect fuel security. Witnesses in this proceeding have raised concerns that permitting Everett to recover all of its costs from ratepayers may:

- Incentivize Everett to over-procure natural gas to satisfy obligations under the Cost of Service Agreement and then dump natural gas into

129 NES-028 at 42:4-12.
130 CT-010 at 8:19-9:26; NES-028 at 42:13-43:22.
131 ENC-0001 at 85:3-18, 103:5-105:4; CT-010 at 7:17-8:1.
132 NEER-001 at 10:6-8.

the market, making it difficult for Everett's competitors, who lack similar subsidization, to compete and potentially push them out of the market.[133] Artificially suppressing the LNG market in this way could have several harmful consequences. First, it eliminates the price signals that trigger infrastructure investment by competing gas suppliers, therefore further harming fuel security in the region. Second, it has the potential to cause other oil-fired plants to either retire or seek cost of service agreements of their own.[134]

- Remove Everett's incentive to pursue economic third-party sales therefore increasing the costs to ratepayers while reducing Everett's efficient operation.[135]

- Incentivize Everett to withhold natural gas from the market thereby raising natural gas prices to the benefit of Exelon's other generating assets.[136]

Mystic witness Schnitzer attempts to discredit these concerns by arguing they are inconsistent and therefore invalid. This misses the point. If Everett benefits from having 100 percent of its fixed and variable costs covered by New England ratepayers, it can act in ways that unsubsidized market participants cannot. How this anticompetitive behavior will manifest can and will change depending on the economic and market conditions of the moment. It is therefore entirely possible and consistent that Everett could behave in each of the above discussed manners at different points during the cost of service period. This is especially true given that this proceeding seeks to establish rates for a two-year period that will not begin until 2022, making it impossible to know with any certainty what market conditions will be in effect at that time.

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[133] NEER-001 at 8; REP-001 at 5; ENC-0052 at 14.
[134] NEER-001 at 10:1-8.
[135] NES-028 at 42-43; CT-010 at 8-9.
[136] ENC-0001 at 82.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

Mystic's arguments in support of its proposal to recover 100 percent of Everett's costs from unwilling New England ratepayers boil down to two basic contentions, neither of which is persuasive. First, that the "interconnected" nature of Everett and Mystic 8 & 9 justifies recovering 100 percent of Everett's fixed and variable costs from Mystic's ratepayers. Second, that LNG from Everett is required for Mystic to satisfy its service obligations during the cost of service period.[137] Both of these arguments ignore the fact that Everett has *always* been the sole source of LNG for the Mystic units and that Everett has been supplying LNG, and recovering its cost, from multiple parties since 1971. Mystic's reliance on the Commission's determination that Everett is "fully integrated with Mystic 8 & 9, and each depends on the other to operate economically" does not support Mystic's proposed cost allocation.[138] That finding went to the Commission's position on jurisdiction (a position that the Massachusetts Attorney General and other parties have contested), and not to cost allocation. In fact, the Commission was explicit in decoupling its statement in support of jurisdiction from any cost recovery determination with respect to Everett, holding that this "finding as to jurisdiction does not mean that Mystic is entitled to recover all costs that it claims in connection with [Everett]. Whether individual components of a cost-of-service rate, including fuel-related costs, are recoverable turns on whether they are just and reasonable."[139]

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[137] MYS-0014 at 21:4-23:11.

[138] *Constellation Mystic Power LLC*, 164 FERC ¶61,022 at P 36 (2018)

[139] *Id.* at P 37.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

Additionally, the "integration" that Mystic asserts is necessary to enable Everett to supply Mystic starting in 2022 is no different or more complex than the integration that has been necessary, and achieved, in supplying Mystic 8 & 9 since they became operational in 2003. Further, Everett has a long history of supplying Mystic's needs while also engaging in third party sales. As discussed above, the majority of Everett's capacity (over 60 percent) will remain available for third party sales even if Mystic 8 & 9 are fully utilized. As a result, Mystic has identified no justification to support its novel and consequential shift away from the Commission's standard cost allocation principles, adoption of which would result in New England ratepayers being saddled with 100 percent of the cost of a facility that uses less than 40 percent of its send out capability to supply natural gas to Mystic 8 & 9. The Commission should reject Mystic's request and allocate no more than 39.16 percent of Everett's costs to Mystic, consistent with the recommendations of NESCOE and the CT Parties.

1. Whether the Fuel Supply Agreement, winter penalties and planning to procure gas for the coldest winter in 50 years create incentives to over-schedule LNG and artificially depress natural gas prices?

See Section B.i.2.a.ii above.[140] The Massachusetts Attorney General agrees that the structure of the Fuel Supply Agreement raises concerning anticompetitive effects that the Commission should take into consideration.[141]

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[140] See discussion associated Mystic's incentive to over procure LNG and then dump on page 37-38.

[141] NEER-001 at 8:3-11; 14:16-15:9.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

2. Whether the Fuel Supply Agreement will create an improper subsidy by ratepayers for third-party natural gas sales?

See Section B.i.2.a.ii above. The Massachusetts Attorney General agrees that the structure of the Fuel Supply Agreement raises concerning anticompetitive effects that the Commission should take into consideration.[142]

3. Whether the costs of owning and operating the Everett Marine Terminal should be allocated between those incurred to service Mystic, on the one hand, and those incurred for third party sales, on the other hand, for purposes of determining cost recovery under the proposed Mystic Cost of Service Agreement?

See Section B.i.2.a.ii above.

4. Whether (i) the proposed percentages of profit to which Constellation LNG and Mystic would be entitled with respect to third-party sales of gas has been justified and (ii) the calculation of any profit sharing incentive for third party sales of gas should be performed *ex post* rather than *ex ante*?

As discussed in Section B.i.2.a.ii above, the need for a profit sharing mechanism can and should be eliminated by following the Commission's customary cost allocation principles and allocating no more than 39.16 percent of Everett's fixed and variable costs to Mystic 8 &9 for recovery from New England ratepayers. To the extent that the Commission decides to adopt Mystic's proposal on this issue, permitting the retention of 50 percent of the margin on forward sales is not

[142] ENC-0001 at 85:3-18; 103:5-105:4.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

justified. The Massachusetts Attorney General supports the position of NESCOE witness Wilson on this issue.[143]

5. Whether ISO-NE should be required to engage a third-party expert to assess the prudency of Mystic's and Constellation's gas procurement and management decisions, and following such assessments, file any disallowances with the Commission under Section 205?

iii. Whether the remaining components of the Monthly Fuel Supply Cost are just and reasonable?

iv. Whether the remaining terms and conditions of the Amended and Restated Fuel Supply Agreement ("FSA") result in rates under the Mystic Agreement that are just and reasonable?

1. Whether the FSA results in just and reasonable fuel charges for Mystic 8 & 9?

See Section B.i.2.a.ii above. The Massachusetts Attorney General supports the position of NESCOE witness Wilson on this issue.[144]

C. Whether the proposed Schedule 3A is just and reasonable, and satisfies the Commission's directive to develop a true-up?

Mystic's proposed Schedule 3A, which reflects its proposed true-up mechanism, is unjust and unreasonable because it is limited to only capital expenditures, O&M, A&G, and property taxes. The Massachusetts Attorney General supports the position of Staff witness Miller that the true-up mechanism must include "all cost components that may be changed absent a section 205 filing"

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143 NES-028 at 43:4-22.
144 NES-028 at 26:19-28:2.

to prevent a potential over recovery by Mystic.[145] The Massachusetts Attorney General additionally supports Ms. Miller's proposed changes to the true-up template to address her concerns.

i. Whether the proposed true-up information exchange process and challenge protocols are just and reasonable?

Mystic's proposed information exchange process and challenge protocols are not just and reasonable. For example, the information exchange process as proposed would not permit parties the ability to evaluate and challenge whether CapEx incurred during the Cost of Service period should more properly have occurred prior to the term. The Massachusetts Attorney General supports the changes proposed by Staff witness Fejka to ensure that parties have access to sufficient information to allow a challenge to the timeliness of project completion.[146] Similarly, the Massachusetts Attorney General shares NESCOE witness Cannady's concern that the time permitted for review is insufficient, and supports the changes proposed in Ms. Cannady's testimony as necessary to ensure the protocols are sufficiently transparent and allow for appropriate time to review and request information.[147]

D. Whether a claw back provision should be adopted, and, if so, what amounts should be refunded and under what circumstances/conditions?

A claw back provision is required to ensure that Mystic's shareholders do not receive a windfall if Mystic 8 & 9 return to the market following the cost of service

[145] S-0034 at 5:14-6:5.
[146] S-0014 at 13:15-14:6.
[147] NES-010 at 25:17-34:12.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

period. Mystic is proposing that any CapEx incurred during the two-year cost of service period be fully expensed and reflected in the proposed cost of service rates. "This full expensing of such costs stands in marked contrast to the way in which such costs are almost invariable treated in traditional cost-of-service ratemaking" where "such CapEx would ordinarily be booked to gross plant in service and generally depreciated over the remaining life of the generating unit."[148] Fully expensing CapEx during the term of the Agreement puts Mystic and Everett at a competitive advantage should they ever return to the market because Mystic's ratepayers "will have effectively paid to upgrade Mystic and [Everett] during the term of the Agreement, only to subsequently provide a windfall to Exelon in any following period of merchant operations."[149] The Massachusetts Attorney General supports the position of ENECOS witness Winterfeld who proposes a claw back mechanism consistent with the one adopted in *New York Independent System Operator, Inc.*, 155 FERC ¶61,076 (2016), *order on reh'g* 161 FERC ¶61,189 (2017) as a Commission recognized way "eliminat[ing], or at least minimz[ing], incentives for a generator needed for reliability to toggle between receiving RMR compensation and market-based compensation for the same unit."[150]

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[148] S-0022 at 7:5-13.

[149] NES-001 at 23:2-7.

[150] *NYISO*,155 FERC ¶61,076 at P 126; ENC-0024 at 24:3-25:13.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

II. Whether the terms and conditions of the Mystic Agreement have been shown to be just, reasonable, and not unduly discriminatory?

A. Whether the Constellation LNG-Constellation Mystic Power LLC Fuel Supply Agreement will enable affiliate abuse or have anticompetitive effects in relevant natural gas and electricity markets?

The Massachusetts Attorney General supports the concerns ENECOS witnesses raised regarding the potential for affiliate abuse and anticompetitive effects associated with the Fuel Supply Agreement as proposed.[151]

III. Whether there are other aspects of the proposed rate to be collected under the Mystic Agreement that are not just and reasonable, and whether additional terms and conditions of the Mystic Agreement, or additional transactional rules should be adopted?

The Massachusetts Attorney General supports the position of NESCOE witness Bentz that the Mystic Agreement contains several deviations from ISO-NE's *pro forma* cost of service agreement in ways that lack clarity and have the potential to harm New England consumers.[152] The Massachusetts Attorney General supports the modifications Mr. Bentz recommends to Sections 2.2 and 2.2.1 regarding termination of the Agreement,[153] Section 2.2.2 establishing the term of the Agreement,[154] Section 3.9 addressing modifications to the Fuel Supply Agreement,[155] and Sections 7.1.1 and 7.1.2 addressing outages.[156]

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151 ENC-0001 at 71:10-106:17; ENC-0052 at 6:1-20:7.
152 NES-001 at 10:9-18.
153 NES-001 at 11:19-16:20.
154 NES-001 at 14:12-16:20.
155 NES-001 at 17:1-18:4.
156 NES-001 at 18:6-21:18.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

CONCLUSION

For the reasons discussed above, Mystic's proposed Cost of Service Agreement is unsupported, deviates from Commission precedent, and produces rates that are unjust and unreasonable. As proposed by Mystic, the Cost of Service Agreement enriches Mystic and Everett while removing all exposure to market risk from the operations of both facilities. New England ratepayers, on the other hand, are saddled with onerous, one-sided terms and excessive and unjust rates. As a result, the Commission should find that Mystic has failed to satisfy its Section 205 burden and reject the filing. Alternatively, the Commission should require Mystic to submit a compliance filing consistent with the Massachusetts Attorney General's above recommendations.

Respectfully submitted,

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20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

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20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Constellation Mystic Power, LLC	)))	Docket No. ER18-1639

PROPOSED FINDINGS OF FACT AND CONLUSIONS OF LAW OF THE ATTORNEY GENERAL OF MASSACHUSETTS

A. Proposed Findings of Fact

FF1. Mystic's proposed gross and net plant values for Mystic 8 & 9 do not reflect the lower of depreciated original cost or Exelon's purchase price, but instead are based on **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]**

FF2. **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]**

FF3. Sithe Energies, Inc. developed Mystic 8 & 9. ENC-0032.

FF4. Mystic 8 & 9 entered commercial operation in 2003 after being acquired by Exelon. ENC-0032 at 2-3.

FF5. In 2003 Exelon took a $573 million impairment against Mystic 8 & 9, which **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]** ENC-0032 at 2-3; Exelon SEC Form 8-K, filed October 23, 2003; Exelon SEC Form 10-Q filed October 29, 2003 at 35-36.

FF6. In 2004 Exelon transferred Mystic 8 & 9, along with other assets, to Boston Generating LLC, a special purpose entity owned by Exelon's lenders, EBG Holdings. ENC-0032 at 3.

FF7. In 2007, ENG Holdings merged with another entity to form US Power Generating Company, **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]**

FF8. As a result **[BEGIN CUI/PRIV-HC]** **[END CUI/PRIV-HC]**

FF9. In 2011 Constellation Energy Group purchased Mystic Units 7, 8, and 9, Mystic Jet, and Fore River from US Power Generating Co. for $1.1 billion. ENC-0032 at 5.

FF10. Constellation **[BEGIN CUI/PRIV-HC]** [redacted] **[END CUI/PRIV-HC]**

FF11. In 2012 Exelon reacquired Mystic 8 & 9 when it merged with Constellation. **[BEGIN CUI/PRIV-HC]** [redacted] **[END CUI/PRIV-HC]**

FF12. Dr. Olson's $2 billion revenue screen is inappropriate because it is unsupported by any analysis or precedent beyond Dr. Olson's personal judgment. S-0011 at 3.

FF13. Sempra must be excluded from any proxy group because its acquisition of Oncor, which occurred during the study period, and because its stock surged by 18 percent following investor reports which recommended the sale of assets. Both of these events impacted Sempra's stock price, which is a DCF input. ENC-0001 at 57:14-16; S-0009 at 3:19-23, 31:23-32:15.

FF14. Avangrid must be excluded from any proxy group because its stock reflects takeover speculation and because its unique position as a controlled company means its financial structure is fundamentally different from Mystic or any other member of the proxy group. S-0013 at 98; S-0010 at 25:21-26:2; ENC-0001 at 27:8-13.

FF15. Dominion must be excluded from any proxy group because its planned acquisition of SCANA negatively impacted its stock price, a DCF input. S-0011 at 22:3-7; S-0013 at 176; ENC-001 at 14:3-7.

FF16. Dr. Olson failed to produce sufficient evidence to support the existence of anomalous capital market conditions. ENC-0001 at 47:17-48:13; ENC-0004.

FF17. The appropriate proxy group consists of twelve utilities and produces a range of reasonableness of 6.81 percent to 10.54 percent. S-0010 at 3.

FF18. During the cost of service period, Mystic will face lower risk than faced by the members of a properly constructed proxy group. ENC-0001 at 66:9-11.

FF19. ExGen's capital structure of 67.28 percent equity/32.72 percent debt is anomalous relative to the capital structures of the proxy group members, who had a range of equity rations from 32.40 percent to 58.70 percent with an average of 48.19 percent. S-0009 at 48:14-20.

FF20. Exelon's capital structure of 48.13 percent equity/51.87 percent debt is the appropriate capital structure to impute to Mystic. CT-001 at 6:14-7:8; S-0009 at 5:1-2.

FF21. Mystic's proposed gross and net plant value for Everett does not reflect the lower of the depreciated original cost or Exelon's acquisition price, because **[BEGINCUI/PRIV-HC]** **[END CUI/PRIV-HC]**

FF22. Exelon's acquisition of Everett **[BEGINCUI/PRIV-HC]** **[END CUI/PRIV-HC]**

FF23. The Mystic 8 & 9 units can use no more than 39.16 percent of Everett's capacity. NES-028 at 26:22-27:2.

B. Proposed Conclusions of Law

CL1. Mystic has failed to carry its Section 205 burden of establishing that the rates it proposes are just and reasonable.

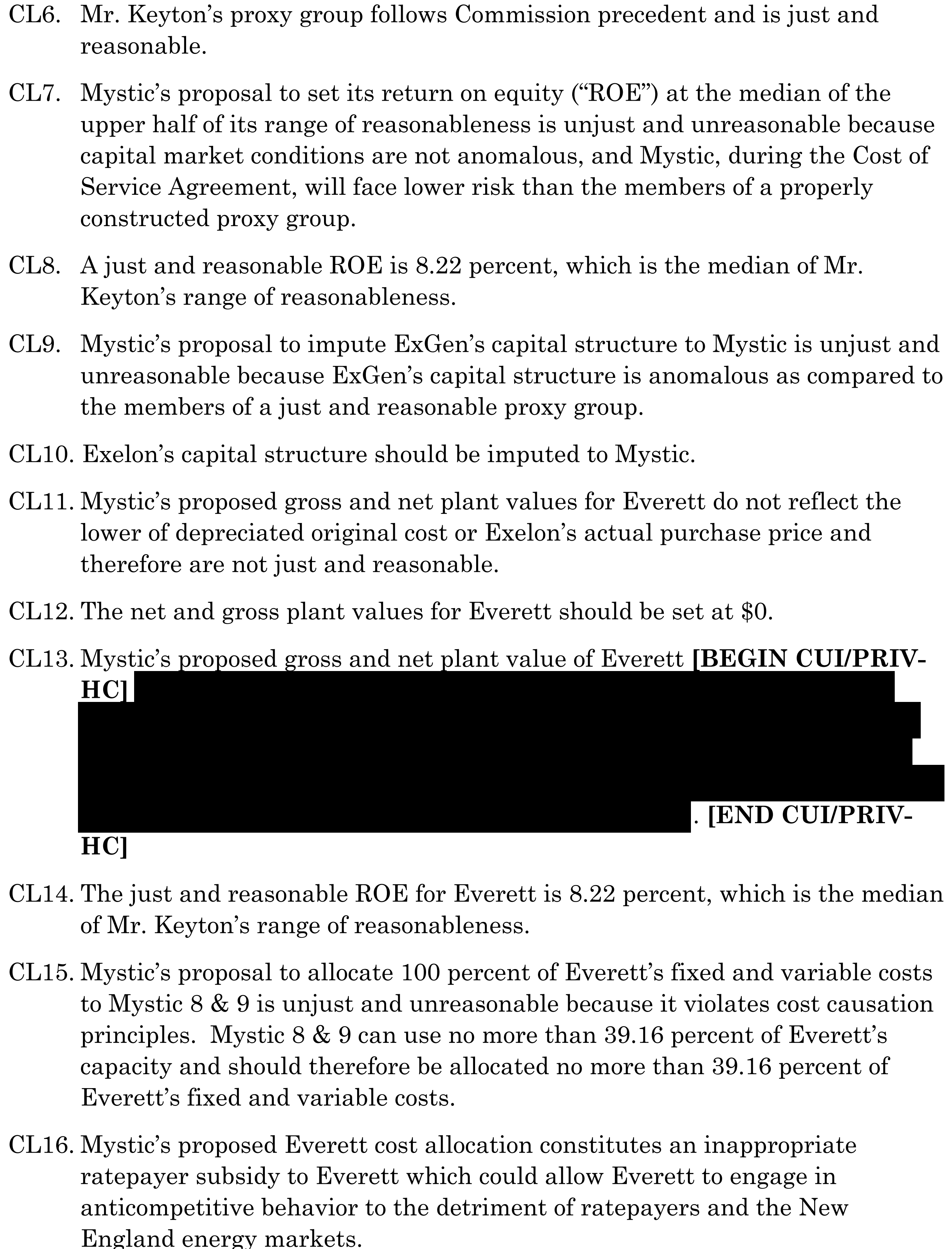
CL2. Mystic's proposed gross and net plant values for Mystic 8 & 9 do not reflect the lower of depreciated original cost or Mystic's actual purchase price and therefore are not just and reasonable.

CL3. Mystic's filing lacks sufficient information to identify the depreciated original cost for Mystic 8 & 9, and it is therefore not possible to apply Commission precedent.

CL4. Mystic's proposed proxy group is unjust and unreasonable because it fails properly apply Commission precedent.

CL5. A proxy group will include only those utilities who; (i) are considered electric utilities by Value Line; (2) have a credit rating no more than one notch above or below the utility whose ROE is at issue; (3) pay dividends and have neither made more announced a dividend cut during the applicable six month study period; (4) have no merger activity during the six month study period that is significant enough to distort study inputs; and (5) whose ROE results pass thresholds tests of economic logic, including both a low-end outlier test and a high-end outlier test.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM



CL6. Mr. Keyton's proxy group follows Commission precedent and is just and reasonable.

CL7. Mystic's proposal to set its return on equity ("ROE") at the median of the upper half of its range of reasonableness is unjust and unreasonable because capital market conditions are not anomalous, and Mystic, during the Cost of Service Agreement, will face lower risk than the members of a properly constructed proxy group.

CL8. A just and reasonable ROE is 8.22 percent, which is the median of Mr. Keyton's range of reasonableness.

CL9. Mystic's proposal to impute ExGen's capital structure to Mystic is unjust and unreasonable because ExGen's capital structure is anomalous as compared to the members of a just and reasonable proxy group.

CL10. Exelon's capital structure should be imputed to Mystic.

CL11. Mystic's proposed gross and net plant values for Everett do not reflect the lower of depreciated original cost or Exelon's actual purchase price and therefore are not just and reasonable.

CL12. The net and gross plant values for Everett should be set at $0.

CL13. Mystic's proposed gross and net plant value of Everett **[BEGIN CUI/PRIV-HC]** . **[END CUI/PRIV-HC]**

CL14. The just and reasonable ROE for Everett is 8.22 percent, which is the median of Mr. Keyton's range of reasonableness.

CL15. Mystic's proposal to allocate 100 percent of Everett's fixed and variable costs to Mystic 8 & 9 is unjust and unreasonable because it violates cost causation principles. Mystic 8 & 9 can use no more than 39.16 percent of Everett's capacity and should therefore be allocated no more than 39.16 percent of Everett's fixed and variable costs.

CL16. Mystic's proposed Everett cost allocation constitutes an inappropriate ratepayer subsidy to Everett which could allow Everett to engage in anticompetitive behavior to the detriment of ratepayers and the New England energy markets.

CL17. Mystic's proposed Schedule 3A is unjust and unreasonable because it fails to true-up all cost components that may be changed absent a Section 205 filing.

CL18. Mystic's failure to include a claw back mechanism is unjust and unreasonable because New England ratepayers will have paid to upgrade Mystic 8 & 9 and Everett during the cost of service period, allowing Exelon a windfall should those units reenter the market. Mystic must adopt a claw back provision consistent with the one adopted in *New York Independent System Operator, Inc.*, 155 FERC ¶61,076 (2016), *order on reh'g* 161 FERC ¶61,189 (2017).

CERTIFICATE OF SERVICE

The undersigned hereby certifies that one copy of the foregoing pleading has this day been served by means authorized under Rule 2010(f) of the Commission's Rules of Practice and Procedure (18 C.F.R. §385.2010(f)) on each person who appears on the Official Service List compiled by the Secretary in this proceeding.

/s/ Ashley M. Bond
Ashley M. Bond
Duncan & Allen

Dated November 2, 2018.

20181102-5228 FERC PDF (Unofficial) 11/2/2018 3:51:40 PM
Document Content(s)

PUBLIC Initial Brief of Mass AGO.PDF................................1-57