

Report of The Committee on Regulations — Parts II and III of The Federal Power Act

I. INTRODUCTION

This report covers the major developments for 1982 in the Commission's regulation of electric utilities under Parts II and III of the Federal Power Act.

In its opinions, the Commission built on its already considerable body of electric ratemaking precedent. It issued major decisions on price squeeze, spent nuclear fuel, transmission cost allocation, revenue credits, rate design and cash working capital. Sensitive to high interest rates, which have been adversely affecting the capital intensive electric utility industry, the Commission generally allowed returns on common equity at or near the high end of the zone of reasonableness.

The Commission proposed a number of important rulemakings. In an effort to provide a more efficient and accurate means for determining return on common equity, the Commission proposed to determine return on equity generically and sever the issue from individual rate cases. In addition, as part of the Reagan Administration's effort to require regulatory agencies to be fiscally self-supporting to the extent possible, the Commission proposed substantial increases in filing fees. Both of these rulemakings, which have received considerable comment, are still pending before the Commission.

The Commission issued several final rules in 1982 which reduce filing requirements for electric utilities. The Commission also reorganized and revised, in part, its Rules of Practice and Procedure in an effort to make its rules more understandable and to expedite proceedings.

In 1982, the federal courts of appeal published over 15 decisions reviewing various actions of the Commission under Parts II and III of the Power Act. The most significant was the decision of the D.C. Circuit vacating two of the Commission's cogeneration rules — namely, that utilities are required to purchase electricity from qualifying facilities at a rate that equals each utility's full avoided cost, and that utilities have the obligation to interconnect with qualifying facilities. The decision is now pending review before the Supreme Court, which has granted certiorari. Most of the other appellate decisions involved standard ratemaking issues. In these decisions, the courts generally deferred to the Commission's expertise and affirmed its ratemaking holdings provided there was record support.

Below, section II discusses the major holdings from the Commission's opinions. Section III briefs the decisions of the courts of appeal reviewing various Commission actions. For convenience, sections II and III are organized, by topic, in digest form. Section IV reviews the major rulemaking activities of the Commission.

II. COMMISSION OPINIONS

A. *Antitrust*

1. *Notice provision*

In *Arizona Public Service Company*, Opinion No. 137, 18 FERC ¶ 61,197, issued March 2, 1982, certain customers of Arizona Public Service claimed that the seven-year notice of termination provisions in their contracts were unlawful. They argued, *inter alia*, that such a provision was anticompetitive in that it restricted their ability to seek alternative sources of power. (See 18 FERC at 61,395). The Commission rejected this claim, finding that the seven-year notice requirement

served the legitimate purpose of adding certainty to the utility's load management planning. (18 FERC at 61,396).

2. *Price squeeze*

The Commission issued a significant decision on price squeeze, in *Pennsylvania Power Company* (Phase II), Opinion No. 157, dated December 21, 1982. There, in considering the appropriate method for determining price discrimination, the Commission rejected the argument that the municipalities were entitled to the same rate as the company's retail industrial customers which had a substantially greater degree of diversity. Instead, the Commission adopted the comparative earned rate of return analysis as the appropriate test for price discrimination. (Slip op. at 3). Under this test, if "the rate of return from wholesale rates exceeds that from the relevant retail rates, price discrimination is shown." (*Id.*) The Commission found that price discrimination existed on the basis of a comparison of the rate of return earned on retail industrial service and that earned on the wholesale service at issue. It further found that the discrimination was of sufficient magnitude and duration to be undue, in the absence of mitigating circumstances.

The Commission, however, did not order a remedy. It found that the discrimination in rates was a result of the dual system of utility rate regulation. Timing differences between the state and federal ratemaking procedures were found to be responsible for the price differential. (Slip op. at 7). The Commission held that "as a general rule we should not lower rates to remedy differences between our ratemaking policies and procedures and those of a state commission." (Slip op. at 6).

3. *Refusal to deal*

In *Electric and Water Plant Board of the City of Frankfort, Kentucky v. Kentucky Utilities Company*, Opinion No. 15-B, 20 FERC ¶ 61,173, issued August 6, 1982, the Commission discussed the circumstances under which the refusal of a utility to discuss coordinating arrangements with an entity that proposed to construct its own generating facilities may constitute undue discrimination. The Commission would require a showing that the proposed "entrant" to the generating business has adequate "preparedness" to enter. (20 FERC at 61,347). It found on the facts before it that Kentucky Utilities' alleged refusal to discuss coordination did not constitute undue discrimination since the City of Frankfort did not have adequate financial ability at the time of the alleged refusal to become a generating utility.

B. *Contracts*

1. *Sierra-Mobile*

In *Central Illinois Public Service Company*, Opinion No. 142, 20 FERC ¶ 61,043, issued July 12, 1982, customers asked the Commission to determine that contracts requiring any rate change be "mutually agreed" upon and approved by the FERC. The Commission ruled that they constitute "open price term" contracts under the Uniform Commercial Code for which a reasonable price may be prescribed. (20 FERC at 61,091). It further ruled that the reasonable rate should be based on fully allocated costs but that the new rate would be prospective only. (20 FERC at 61,092).

In *Public Service Company of New Mexico*, Opinion No. 133-A, 18 FERC ¶ 61,036,

issued January 29, 1982, the Commission held that the appropriate effective date for a rate increase to a Section 206 customer is the date of the final Commission order, not the date of the compliance filing.

C. *Cost of Service*

1. *Allowance for funds used during construction*

In *Southern California Edison Company*, Opinion No. 145, 20 FERC ¶ 61,301, issued September 10, 1982, the Commission allowed Edison to use a net-of-tax AFUDC rate in order to be consistent with its retail rate method. As the Commission observed, “[t]he . . . policy concerning gross-of-tax/net-of-tax AFUDC is that the gross-of-tax method should be utilized unless the net-of-tax method is prescribed by another regulatory body in setting rates for the subject utility.” (20 FERC at 61,587).

2. *Cash working capital*

In *Public Service Company of New Mexico*, Opinion No. 146, 20 FERC ¶ 61,290, issued September 17, 1982, the Commission addressed for the first time the question of whether a negative figure resulting from a fully developed and reliable lead-lag study should be deducted from the cash working capital component of rate base. The Commission chose not to order a negative cash working capital allowance and instead fixed the allowance at zero. It ruled that “a rate base deduction should not be made without further analysis and careful consideration of the matter.” (20 FERC at 61,550). It reached the same conclusion in *Minnesota Power & Light Company*, Opinion No. 155, issued November 30, 1982, at 3.

In *Southern California Edison Company*, Opinion No. 145, 20 FERC ¶ 61,301, issued September 10, 1982, the Commission held that the proposed overall rate of return, rather than a past earned return, should be used for calculating the income tax component in the cash working capital lead-lag study. In addition, it held that ratably flowed-through investment tax credits should not be netted against income taxes payable in deriving the tax component of cash working capital, except in the year the credits arise (20 FERC at 61,591).

In *Pacific Gas and Electric Company*, Opinion No. 147, 20 FERC ¶ 61,340, issued September 22, 1982, the Commission held that non-cash items such as depreciation should be excluded from the cash working capital allowance.

3. *Contributions*

In *Wisconsin Power & Light Company*, Opinion 141, 19 FERC ¶ 61,288, issued June 23, 1982, the Commission reaffirmed its position that contributions to Edison Electric Institute are allowable except to the extent that they are channelled to lobbying activities, the Electric Power Research Institute or the Liquid Metal Fast Breeder Reactor Program. (19 FERC at 61,569).

4. *Cost allocation*

a. *General*

The central question in *Town of Highlands, North Carolina, et al. v. Nantahala*

Power and Light Company, Opinion No. 139, 19 FERC ¶ 61,152, issued May 14, 1982, was whether the rates for two wholly owned electric power subsidiaries of Alcoa (Nantahala and Tapoco, Inc.) should be set by rolling in the costs of the two systems. Nantahala and Tapoco together receive entitlements for power generated by TVA-operated hydroelectric projects along the Little Tennessee River, and these entitlements are then allocated between the two systems according to an apportionment agreement. Under the apportionment agreement Tapoco, which is the power supply source for Alcoa's aluminum smelting operations in Tennessee, receives the lion's share of the entitlements. Nantahala serves a public utility load in western North Carolina.

Certain customers of Nantahala filed a complaint urging that the Commission pierce the corporate veil and combine the costs of the Nantahala and Tapoco systems for ratemaking purposes. The Commission declined to do so, since it could not find that "Alcoa has used the separate corporate identities of Nantahala and Tapoco to frustrate the purposes of the Federal Power Act, or that the two companies operate as an integrated system." (19 FERC at 61,277). Nevertheless, the Commission did hold that the apportionment agreement by which entitlements to TVA power are allocated between the two subsidiaries was unfair, and it set Nantahala's portion of the entitlements equal to a proportionate amount of its actual contribution of power to TVA. (19 FERC at 61,278-80).

b. *Demand costs*

In *Arizona Public Service Company*, Opinion No. 137, 18 FERC ¶ 61,197, issued March 2, 1982, the Commission considered the appropriate demand projection for a customer having a take-or-pay provision in its contract. The Commission held that the demand attributed to the customer should not be a projection based on the load it was expected to take, but rather should be the load established by the take-or-pay provision. (18 FERC at 61,391).

c. *Distribution costs*

In *Arizona Public Service Company*, Opinion No. 137, 18 FERC ¶ 61,197, issued March 2, 1982, the Commission approved the allocation of distribution costs by use of non-coincident demands for each district served by the company rather than by use of the combined demands of the districts. The theory was that "the distribution facilities are designed to meet the individual load projected for that load center." (18 FERC at 61,391).

d. *Transmission costs*

In *Pacific Gas and Electric Company*, Opinion No. 143, 20 FERC ¶ 61,190, issued August 16, 1982, Staff and certain Intervenors argued that PGandE's rate for transmitting power for the Central Valley Project (a federal system) should be based on combining the costs of the PGandE and CVP transmission systems. The Commission rejected this argument finding that while the PGandE and CVP systems were "operationally" integrated, PGandE did not materially benefit from the CVP system, which was planned and constructed independently of PGandE. Thus, the Commission concluded the combined system method would, unfairly, shift costs to PGandE's other ratepayers.

In *Florida Power & Light Company*, Opinion No. 152, 21 FERC ¶ 61,070, issued November 10, 1982, the City of New Smyrna Beach argued that FP&L and Florida Power Corporation should file a joint (through) rate for the wheeling service. The Commission rejected this proposal on the ground that it need not order joint rates unless the individual rates are unjust and unreasonable and the utilities have a duty to wheel the power. (21 FERC at 61,240). It expressed a reluctance to approve a transmission rate for the City that was less than what other customers were paying. Moreover, as for the appropriate transmission rate base, the Commission adopted a rolled-in costing approach and rejected the theory that a transmission customer should not have to pay for transmission costs allegedly associated with the “generation reliability” function. (21 FERC at 61,241-2).

The *Florida Power & Light* decision also dealt with the appropriate rates for the company’s transmission service for short-term energy exchanges between several Florida cities and other utilities. The Commission again rejected a proposal that FP&L and FPC should file a joint rate applicable to their combined wheeling services in regard to these transactions. The Commission modified the “save harmless” clause in the transmission service agreements so that FP&L could be held liable for interruptions in deliveries due to its negligence or willful misconduct; it criticized as vague the “reactive power” clause in FP&L’s tariff which permitted FP&L to interrupt service when the customer’s power factor was not “as near unity as practical”; and it allocated some demand costs to the transactions, although it ruled that none of them were firm. (See 21 FERC at 61,243-5).

An issue arose in *Southern California Edison Company*, Opinion No. 145, 20 FERC ¶ 61,301, issued September 10, 1982, over the allocation of costs associated with two 66 Kv lines each of which currently serves only one customer. The Commission required these lines to be rolled in as part of the integrated transmission network rather than functionalized as distribution facilities since they have the capacity to serve additional customers. (20 FERC at 61,588-89). The losses over these lines were also required to be allocated on a rolled-in basis for consistency. (*Id.*)

5. *Extraordinary property losses*

In *Wisconsin Power & Light Company*, Opinion No. 141, 19 FERC ¶ 61,288, issued June 23, 1982, the company suffered a loss of part of its plant during the test period because of an ice storm. The parties agreed that the loss should be recovered over a five year amortization period, but an issue was raised over how to treat the reduction in income taxes resulting from the loss. The intervenors proposed that the tax reduction be booked to Account No. 283 (Accumulated Deferred Income Taxes) and flowed back to ratepayers over the five-year amortization period, with the unamortized balance in Account No. 283 being deducted from rate base. The unamortized portion of the loss, however, would not be included in rate base; thus, this proposal would deny the company a return on that portion of its rate base equal to the reduction in tax liability. The Commission rejected the intervenors’ proposal on the ground that it would shift too much of the loss to shareholders, contrary to the policy of an equitable sharing of losses between shareholders and consumers established in *New England Power Company*, Opinion No. 49, issued July 19, 1979, *New England Power Company*, Opinion No. 49, issued July 19, 1979, *aff’d sub nom.*, *NEPCO Municipal Rate Committee v. FERC*, 668 F.2d 1327 (D.C. Cir. 1981), *cert. denied*, 102 S. Ct. 2928 (1982).

6. *Fuel adjustment clause*

In *Commonwealth Edison Company*, Opinion No. 63-B, 20 FERC ¶ 61,368, issued September 23, 1982, the Commission held that the company's use of a fuel adjustment clause that did not conform to Order No. 517 would not necessitate refunds so long as the aggregate revenues produced by the base rates and the fuel clause were just and reasonable. In other words, in determining refund liability, undercollections under the base rates can offset overcollections under the fuel clause.

7. *Nuclear costs*

a. *Decommissioning*

In *Southern California Edison Company*, Opinion No. 145, 20 FERC ¶ 61,301, issued September 10, 1982, the Commission rejected, for lack of sufficient evidence, a proposed change in Edison's depreciation accrual rates designed to include decommissioning costs for the San Onofre Nuclear Unit No. 1. (20 FERC at 61,591-92).

b. *Spent fuel*

For the first time, in *Boston Edison Company*, Opinion No. 156, 21 FERC ¶ 61,327 issued December 23, 1982, the FERC permitted a utility to recover in present rates the estimated costs of disposing of spent nuclear fuel. The Commission abandoned its previous position that spent fuel was a valuable asset that would eventually be reprocessed, finding the evidence now showed that spent fuel "will have a negative salvage value regardless of the federal policy on reprocessing." (21 FERC at 61,879). The Commission reasoned that present customers should pay the costs that eventually must be incurred in disposing of nuclear fuel used for their benefit.

8. *Purchase power expense*

In *Wisconsin Power & Light Company*, Opinion No. 141, 19 FERC ¶ 61,288, issued June 23, 1982, the Commission rejected a proposed allowance of some \$1 million for unplanned outages as part of the company's purchased power expense. This decision was based on the fact that the company's reserve capacity was sufficient to eliminate any need for purchases of power during periods of unplanned outages. (19 FERC at 61,569).

9. *Revenue credits*

In *Public Service Company of New Mexico*, Opinion No. 146, 20 FERC ¶ 61,290, issued September 17, 1982, the Commission held that a revenue credit rather than cost allocation should be used for opportunity sales to the City of Los Angeles. The Commission found that cost allocation is not feasible for opportunity sales because of their unpredictability.

In *Pacific Gas and Electric Company*, Opinion No. 147, 20 FERC ¶ 61,340, issued September 22, 1982, at issue was a 1966 fixed rate contract in which PGandE sold power to the California Department of Water Resources (DWR) at 3 mills per kwh for pumping water in the California Aqueduct. Under another contract, DWR sold

power generated at DWR's Feather River Hydroelectric project to PGandE. The Commission held that PGandE was entitled to a revenue credit for its below cost sales to DWR because at the time the contracts were entered into, PGandE expected that it would receive a net benefit and there was no evidence that PGandE had acted imprudently.

10. *Tax expense*

In *Arizona Public Service Company*, Opinion No. 137, 18 FERC ¶ 61,197, issued March 2, 1982, it appeared that the company's investment tax credits from investments in new electric generation and transmission facilities were sufficient to result in a negative tax liability. The Commission ruled that this negative tax liability should be reflected in rates since the company had elected to flow through all its investment tax credits to its customers. (18 FERC at 61,392). On rehearing, however, it was shown that the company's calculation of a negative tax liability was in error and that a positive tax liability existed for all customer groups; accordingly the issue of a negative tax liability was mooted. Opinion No. 137-A, 20 FERC ¶ 61,407, issued September 30, 1982.

In *Public Service Company of New Mexico*, Opinion No. 146, 20 FERC ¶ 61,290, issued September 17, 1982, the Commission approved the inclusion in cost of service of the state gross receipts tax over the objection that the tax was unconstitutionally applied. It held that the question of the lawfulness of the tax was beyond the Commission's jurisdiction. (20 FERC at 61,549).

In *Southern California Edison Company*, Opinion No. 145, 20 FERC ¶ 61,301, issued September 10, 1982, an issue was raised as to whether the company should flow through to ratepayers certain tax benefits not normalized by the time of removal of the asset. Traditionally, when an asset is removed at the end of its useful life the removal cost is tax deductible. To normalize this tax benefit, a *pro rata* share of the benefit is accorded the ratepayers during each year of service life. The Commission ruled that since Edison has, in the aggregate, unfunded future tax liability, the excess funds in the deferred tax account associated with removal costs should be used to make up the aggregate unfunded liability. (20 FERC at 61,588).

D. *Discrimination*

In *Wisconsin Power & Light Company*, Opinion No. 141, 19 FERC ¶ 61,288, issued June 23, 1982, the Commission addressed allegations of undue discrimination, between the wholesale rates in question and WP&L's rates to South Beloit Water, Gas and Electric Co. (SBWG&E), a wholly owned subsidiary of WP&L. WP&L provides retail service to the City of Beloit, Wisconsin, and SBWG&E provides retail service to the City of South Beloit, Illinois. South Beloit is separated from its sister city by a paved street, the center of which is the state line. The entire metropolitan area, however, is served from a single integrated distribution system. Wholesale customers of WP&L alleged that the rates to SBWG&E were so low as to be unduly discriminatory.

The Commission rejected this allegation. First, it found that although WP&L may achieve a low rate of return on its wholesale sales to SBWG&E, SBWG&E may have a high rate of return on retail service, indicating that at the retail level other utilities would not be disadvantaged in competing with SBWG&E. Second, it found that the complaining customers are not in proximity to SBWG&E and thus they

would not be competitively disadvantaged. (19 FERC at 61,568). Third, it found SBWG&E is not a functionally independent utility, and so the service it receives from WP&L is not the same as the service received by the other customers. (*Id.*).

Central Illinois Public Service Company, Opinion No. 142, 20 FERC ¶ 61,043, issued July 12, 1982, addressed the question of discrimination between the cooperative customers who had reached a settlement with the company and municipal customers who had chosen to litigate. The Commission first ruled that the Presiding Judge had erred in applying price squeeze standards to such a discrimination claim since the price squeeze presumptions are not appropriate where a higher standard of proof on competitive harm is involved. (20 FERC at 61,087-8). The Commission analogized this case to a case where discrimination is alleged to arise out of the use of fixed-rate and variable-rate contracts and ruled that no undue discrimination is present simply because one group of customers has settled while another has not. (See 20 FERC at 61,088; Opinion No. 142-A, 20 FERC ¶ 61,435, issued September 30, 1982).

E. *Filed rate doctrine*

In *Pennsylvania Power Company*, Opinion No. 157, (Phase II) 21 FERC ¶ 61,313, issued December 21, 1982, the Commission held that the company could not recover uncollected revenues which resulted from a computational error in the cost of service. To do so, the Commission said, would violate the filed rate doctrine and the rule against retroactive ratemaking. (Slip op. at 8).

F. *Rate design*

1. *Customer class*

A definitive statement on the subject of customer classes was issued in *Central Illinois Public Service Company*, Opinion No. 142, 20 FERC ¶ 61,043, issued July 12, 1982. There the Commission approved the use of separate rate classes for the cooperative and municipal customers of CIPSCO. Its starting point was the proposition that overclassification (i.e., numerous separate classes) is preferable to underclassification. The Commission reasoned that even if customers who impose identical costs on the utility are incorrectly separated into different classes, they will still be charged identical rates so long as uniform cost of service methods are employed. (20 FERC at 61,085-6). In short, the Commission has taken a position in favor of establishing separate rate classes for customer groups where it appears that the costs of serving them may be different.

2. *Demand ratchets*

In *Central Illinois Public Service Company*, Opinion No. 142-A, 20 FERC ¶ 61,435, issued September 30, 1982, proposed demand ratchets for both full requirements customers and customers with their own generation were rejected. The Commission found that the company had not made a sufficient showing that either group of customers would deviate so significantly from the test-period projection of billing demands that the recovery of demand costs would be jeopardized. (20 FERC at 61,886).

In *Minnesota Power & Light Company*, Opinion No. 155, 21 FERC ¶ 61,233, issued November 30, 1982, by contrast, a demand ratchet for partial requirements

customers was found appropriate. Following Opinion No. 81, the Commission indicated that a utility using the 12 CP method of demand allocation may also impose a demand ratchet on customers if the benefits outweigh the disadvantages. As the Commission observed, “partial requirements customers have the opportunity to utilize alternative sources of capacity to control their load on MP&L’s system. So, the ratchet is appropriate to compensate the utility for capacity it must hold ready for the use of its partial requirements customers in the event they choose to take it.” (21 FERC at 61,522).

3. *Time of use rates*

In *Southern California Edison Company*, Opinion No. 145, 20 FERC ¶ 61,301, issued September 10, 1982, the Commission approved Edison’s rate design by which wholesale customers have the option of being served under a time-of-use rate schedule. In doing so, the Commission rejected the Administrative Law Judge’s decision to establish, essentially, a separate class for each customer, with a time-of-use option for all of them. It also rejected the proposal of one customer to establish two rate classes for wholesale customers — a high diversity time-of-use class and a low diversity class. (20 FERC at 61,593-4).

G. *Rate of Return*

The Commission issued several decisions concerned with the proper rate of return on equity, although none of these decisions contained much in the way of discursive reasoning. A list of these decisions, with the principal reasons for the result indicated in parentheses, follows.

— *Arizona Public Service Company*, Opinion No. 137, 18 FERC ¶ 61,197, issued March 2, 1982 (15% allowed for the locked-in period August 1, 1979 to August 1, 1981 because of significant changes in the company’s financial posture and in the financial markets generally; the company’s bonds had been downgraded after the close of the record (18 FERC at 61,400)).

— *Town of Highlands, North Carolina, et al. v. Nantahala Power and Light Company*, Opinion No. 139, 19 FERC ¶ 61,152, issued May 14, 1982 (13% allowed — while the Commission found that Nantahala was a “low-risk company”, it emphasized the volatile money market conditions during the locked-in period, October 1, 1976 to March 1, 1981 (19 FERC at 61,286)).

— *Wisconsin Power & Light Company*, Opinion No. 141, 19 FERC ¶ 61,288, issued June 23, 1982 (13.1% allowed for the locked-in period May 2, 1977 to October 1, 1980 on the basis of increased costs of debt during the latter part of the locked-in period (19 FERC at 61,569)).

— *Pacific Gas and Electric Company*, Opinion No. 143, 20 FERC ¶ 61,190, issued August 16, 1982 (13.5% allowed for transmission service for the locked-in period April 1, 1976 to March 31, 1981, stressing that it balanced the market conditions for the entire locked-in period).

— *Southern California Edison Company*, Opinion No. 145, 20 FERC ¶ 61,301, issued September 10, 1982 (the Commission allowed 14.6% on equity, noting that the prime rate had been above 20% during the locked-in period August 16, 1979 to July 16, 1981 (20 FERC at 61,590-1)).

— *Pacific Gas and Electric Company*, Opinion No. 147, 20 FERC ¶ 61,340, issued September 22, 1982 (15% on equity based on a 1980 test year; Commission declined to decide whether equity is riskier than debt based on the evidence presented).

— *Minnesota Power & Light Company*, Opinion No. 155, 21 FERC ¶ 61,233, issued

November 30, 1982 (14.9% on equity was authorized based on a DCF analysis of comparable utilities; the Commission also stressed the high cost of debt during the effective period of the rates from June 1, 1980 to November 1, 1981, which has a "particularly adverse effect on the capital intensive utility industry" (21 FERC at 61,520)).

In *Connecticut Yankee Atomic Power Company*, Opinion No. 148, 20 FERC ¶ 61,373, issued September 28, 1982, the Commission considered the appropriate return from unit sales by a single-asset nuclear generating company, jointly-owned by several New England utilities. The Commission, affirming the Administrative Law Judge, held that the rate of return for the company should be set on a "stand-alone" basis. It thereby rejected the Staff's proposal to use the cost of capital for each of the parent companies as the measure of the fair return. Connecticut Yankee was viewed as being a higher risk enterprise than its parents since it is a single-asset nuclear facility, which eventually will face high decommissioning costs. In addition, the purchasers of its output are entitled to cancel their obligations if a prolonged outage occurs. (See 20 FERC at 61,766-7). Accordingly, the Commission approved a rate of return on equity of 17%.

III. COURT OPINIONS

Discussed below are the major decisions of the federal courts of appeal in 1982 reviewing the decisions of the Commission under Parts II and III of the Federal Power Act.

A. *Jurisdiction of the Commission*

State of Utah et al. v. Federal Energy Regulatory Commission, 691 F.2d 444 (10th Cir. 1982)

The court upheld the Commission's determination that it had exclusive jurisdiction over the sale of wholesale power by Utah Power & Light Company to Sierra Pacific Power Company. Dissatisfied with the FERC's rate treatment for this sale, the Utah Public Service Commission sought jurisdiction over the sale on the ground that it had jurisdiction over the facilities used to generate the power. In affirming the FERC, the court pointed out that, if the terms of the contract operate to the detriment of Utah customers, the FERC has authority to modify the agreement in the public interest.

B. *Ripeness for Appellate Review*

Cities of Anaheim and Riverside, California v. Federal Energy Regulatory Commission, 692 F.2d 773 (D.C. Cir. 1982)

This was an appeal from a series of Commission orders relating to the licensing of the Balsam Meadow hydroelectric project which is located in central California between two existing projects licensed to Southern California Edison. Edison filed a preliminary permit application for the project in September 1978, and shortly thereafter the Cities of Anaheim and Riverside filed a competing permit application. Edison then filed to withdraw its permit application and instead to amend one of its existing licenses to include the Balsam Meadow development as part of the project. The Commission accepted Edison's application and notified the

Cities that they would have to file a competing license application. The Cities appealed this ruling, contending that the Commission's action denied them the right to a comparative hearing on their permit application and deprived them of the municipal preference under Section 7(a) of the Power Act.

The D.C. Circuit, however, ruled that the Commission orders were not ripe for review. It reasoned that the orders lacked finality in that they were procedural and did not determine substantive rights, that the Cities had not suffered irreparable injury, and that judicial review at this stage of the proceedings would invade the province of the Commission to decide the merits of the licensing controversy.

C. *Suspension Orders*

1. *Delmarva Power & Light Company v. Federal Energy Regulatory Commission*, 671 F.2d 587 (D.C. Cir. 1982)

In this case, the D.C. Circuit dismissed challenges by Delmarva and its customers to a series of suspension orders issued by the Commission suspending a two-phase rate increase filed by Delmarva Power & Light.

The court held that the Commission action was unreviewable. It stated that an agency's decision to accept a rate filing, as well as the length of the suspension period, were matters "utterly inappropriate for judicial review" absent substantial prejudice to a party (671 F.2d at 594). It emphasized that the Commission's action was interlocutory in nature and that no party is likely to suffer irreparable harm in view of the imminence of a hearing and the availability of the refund remedy.

2. *Southern California Edison Company v. Federal Energy Regulatory Commission*, 686 F.2d 43 (D.C. Cir. 1982)

The court upheld the Commission decision to suspend Southern California Edison's proposed two-step rate increase for the full five-month statutory period. Relying upon *Delmarva Power & Light, supra*, it held that once it has determined, as here, that the Commission had adequately articulated its reasons for the suspension, it is inappropriate for a reviewing court to go further and examine the merits of why the Commission chose a particular suspension period.

D. *Effective Date of Rate*

Kentucky Utilities Company v. Federal Energy Regulatory Commission, 689 F.2d 207 (D.C. Cir. 1982)

Kentucky Utilities challenged a Commission order suspending its proposed rate increase for five months and 21 days after the proposed effective date. The company argued that the Commission had no authority to delay the effectiveness of the rates for a period longer than five months and that the Commission had failed to give adequate reasons for imposing the maximum suspension period. The filing date of the company's rate increase had been delayed by the Commission because of certain deficiencies in the original filing.

The D.C. Circuit upheld the Commission's action. It ruled that the Commission had acted properly in regarding the original filing as deficient and in delaying the assignment of the filing date until the deficiency was corrected. In addition, the court ruled that the Commission had supplied adequate reasons for imposing the

maximum suspension period under the court's earlier decision in *Southern California Edison C. v. FERC*, 686 F.2d 43 (D.C. Cir. 1982).

E. Cogeneration and Small Power Production Facilities

American Electric Power Service Corporation v. Federal Energy Regulatory Commission, 675 F.2d 1226 (D.C. Cir. 1982), *reh. denied*, No. 80-1789 (filed April 23, 1982), *cert. granted*, 74 L.Ed.2d 165*

The Supreme Court has granted petitions for a writ of certiorari to review this decision which considered several challenges to the FERC's rules implementing the cogeneration and small power production provisions of the Public Utility Regulatory Policies Act, 16 U.C. 2606 (1978) ("PURPA"). The first challenge was to the requirement imposed by the FERC that utilities purchase electricity from qualifying facilities at a rate that equals each utility's full avoided cost. The court of appeals vacated and remanded the full avoided cost rule, finding that the Commission had not adequately established that the rule would be "just and reasonable to the electric consumers of the electric utility and in the public interest" as required by § 210(b) of PURPA. (675 F.2d at 1232.) The court directed the Commission to take a harder look at whether rates based on some percentage of avoided costs would provide a more equitable sharing of benefits of cogeneration and small power production.

The court rejected challenges to the FERC's simultaneous purchase and sale rule. Under this provision, new qualifying small power producers and cogenerators are allowed to engage in the fiction that the power they generate is simultaneously purchased by the utility and sold back to the qualifying facility at retail rates. The purpose of this rule is to prevent discriminatory treatment between qualifying facilities that consume the power they generate and those that actually sell to the utility. The court ruled that the Commission had adequately considered the impact of its rule on all interested parties.

The court vacated, however, the Commission's rule imposing an obligation on all electric utilities to interconnect with qualifying facilities. Section 210(e) (3) of the Federal Power Act provides that qualifying facilities are not to be exempted from Sections 210, 211 and 212 of the Act which establish certain standards and safeguards concerning interconnections and wheeling. The D.C. Circuit held that the Commission's interconnection requirement had the effect of exempting qualifying facilities from the provisions of Sections 210 and 212 of the Act, in direct contravention of Section 210(e) (3).

Finally, the court of appeals upheld the Commission's decision not to establish fuel use criteria for qualifying cogeneration facilities. The petitioners in the case had advocated criteria aimed at limiting oil- and gas-fired cogeneration. The court ruled that PURPA gave the Commission discretion to determine whether to adopt fuel use criteria, and that the Commission had valid reasons for not adopting such criteria especially in light of its strict fuel efficiency standards for gas- and oil-fired cogenerators.

F. Ratemaking Issues

1. Undue discrimination — *Alabama Electric Cooperative, Inc. v. Federal Energy Regulatory Commission*, 684 F.2d 20 (D.C. Cir. 1982)

*Editor's Note: On May 16, 1983, the Supreme Court reversed the D.C. Circuit's decision and remanded the case. — U.S. —, 51 U.S.L.W. 4547, decided May 16, 1983.

The cooperative customers of Alabama Power had argued that the use of a single rate class applicable to themselves and the company's municipal customers resulted in unduly discriminatory rates. They pointed out that the application of a single rate class produced a disparity in the company's rate of return of .45 percent as between the cooperatives and municipalities. The FERC refused to address this discrimination issue on the ground that it was raised too late in the proceedings.

The D.C. Circuit, ruling that the issue had been timely raised, remanded the case for full consideration of the cooperatives' objections. The court held that applying the same rate to customers with different cost characteristics constitutes undue discrimination.

2. Inclusion of "practices" in economy energy tariff — *The Village of Winnetka, Illinois v. Federal Energy Regulatory Commission*, 678 F.2d 354 (D.C. Cir. 1982).

The Village of Winnetka purchased large quantities of economy energy from Commonwealth Edison from 1972 until June 6, 1979. During this period Comm Ed made economy energy available to Winnetka except when Comm Ed's highest-cost generating units were in operation. Comm Ed would notify Winnetka daily at 5 a.m. of the projected time periods during which economy energy would be available in the ensuing twenty-four hours. On June 6, 1979, Comm Ed unilaterally changed the conditions governing economy energy sales, to provide that such power would be available only during hours when none of its oil-fired generators were in use. Notification would be made twice daily concerning economy energy availability during the ensuing twelve-hour period.

Winnetka filed a complaint with the FERC seeking to compel Comm Ed to amend its tariff to reflect the 1972-1979 practice regarding economy energy sales, not to depart from this practice without prior FERC approval, and to refund the additional charges Winnetka had paid under the more restrictive conditions. Winnetka's position was that the standards previously followed by Comm Ed were "practices" within the meaning of Section 205(c). The FERC dismissed the complaint on the ground that Comm Ed's tariff gave it "sole authority" to determine the availability of economy energy.

On appeal the D.C. Circuit vacated the Commission's order and remanded the case. It ruled that the FERC had not clearly set forth the grounds for its decision. The court stated:

... If the FERC determined that Comm Ed's 1972-1979 economy energy procedures were not "practices" within the meaning of section 205(c), it should explain why it reached that conclusion. Similarly, if the FERC believes its "rule of reason" exempts specific economy energy sale terms from inclusion in a utility's tariff, it should state why it arrived at such a decision. 678 F.2d at 357.

3. Inclusion of Construction Work in Progress in rate base — *El Paso Electric Company v. Federal Energy Regulatory Commission*, 667 F.2d 462 (Former 5th Cir., Unit A, 1982)

This review proceeding primarily concerned whether the Commission had acted properly in denying El Paso Electric's proposal to include CWIP in rate base.

El Paso had sought rate base inclusion of CWIP on the ground of severe financial distress, but the Commission relied on the fact that the Texas PUC, which regulates 78% of the company's total annual sales, had allowed the inclusion of CWIP in rate base and thereby alleviated El Paso's financial distress. El Paso argued that it was impermissible for the Commission to consider its non-jurisdictional

business in determining whether CWIP relief was appropriate for that part of the company's business (4%) that is subject to federal regulation. The court, however, upheld the Commission's denial of CWIP relief. Noting that CWIP relief is an extraordinary remedy, it ruled that the Commission should not "close its eyes to other aspects of a utility's operations in determining if a company suffers 'severe financial distress'" (667 F.2d at 469.)

4. Depreciation, rate of return, transmission costs and cash working capital — *Cities of Aitkin et al. v. Federal Energy Regulatory Commission*, No. 80-2375 (D.C. Cir., March 5, 1982).

The court first upheld the Commission in permitting an increase in the rate of depreciation claimed for steam and hydraulic generating equipment. Second, with respect to rate of return, the court rejected the customers' argument that the Commission should have prescribed a lower return on wholesale business than on retail business because of the comparatively lower degree of risk associated with the wholesale provision of power. It was held that the Commission acted properly in refusing to inquire into this alleged difference in risks.

The court also rejected the wholesale customers' claim that the cost of subtransmission facilities used to connect them to the main system should be rolled in with system-wide transmission costs. It found that the Commission properly allocated these costs to the wholesale customers since the evidence showed that the subtransmission lines could not physically be used to benefit any other users.

The court remanded to the Commission the question of the appropriate working capital allowance. The Commission had rejected the customers' lead-lag study on the ground that it failed to reflect *actual* data as to the receipt of payments from customers; instead, it applied the 45-day formula. The court ruled that the Commission had not adequately explained its decision to reject the lead-lag study.

5. Plant abandonment — *South Dakota Public Utilities Commission et al. v. Federal Energy Regulatory Commission*, 690 F.2d 675 (8th Cir. 1982).

The South Dakota Public Utilities Commission and the Minnesota Public Utilities Commission challenged the Commission's decision allocating the abandonment costs of Northern States Power Company's Tyrone nuclear station. The FERC decided that, in accordance with the coordinating agreement between NSP (Minnesota) and NSP (Wisconsin), 87% of the costs arising out of the cancellation of the Tyrone plant should be allocated to NSP (Minnesota), with the balance allocated to NSP (Wisconsin).

The court affirmed the findings of the FERC that, *inter alia*, the allocation between the two companies did not unduly favor the state of Wisconsin and that the use of a 10-year amortization period for recovering the loss, as opposed to the 30-year period supported by South Dakota and Minnesota, was fair.

6. Reserve capacity, fuel adjustment clause, demand allocation and price squeeze — *Cities of Batavia et al. v. Federal Energy Regulatory Commission*, 672 F.2d 64 (D.C. Cir. 1982)

The court first upheld the Commission's determination that Comm Ed's generating reserve capacity of 30.8% during the test year was not excessive. Municipal customers of Comm Ed had argued that generating capacity during the test year was 12.9% higher than normal for the longer period during which the

proposed rate would be effective, and that therefore the Commission should require a “normalizing” adjustment to the reserves allowed in test year rate base in order to effect an averaging of excess capacity. The court, however, adopted the Commission’s view that Comm Ed’s reserve capacity did not require a departure from the test year approach since increased costs to serve increased demand can be expected subsequent to the test year.

An issue was also raised concerning the company’s fuel adjustment clause that was in effect at the time of its 1974 rate filing. That fuel clause reflected losses on a total system basis rather than on a wholesale basis as required by the regulations. At the time of the 1974 filing the Commission refused to suspend the fuel clause, since it had been previously accepted, and instead instituted a Section 206 investigation. In 1975 the company filed a new fuel clause that conformed to Order No. 517, and the Commission terminated the Section 206 investigation. On appeal, the D.C. Circuit reversed the Commission’s decision not to suspend the fuel clause at the time of the 1974 filing and remanded the case to allow the Commission to consider “whether the old fuel adjustment clause interacted so differently in the context of the revised schedule that it effected an unjust and unreasonable rate and, if so, to determine whether this is an appropriate case in which to exercise its Section 205 suspension and refund jurisdiction.” (672 F.2d at 77).

The court also affirmed the Commission’s decision to adopt a 1-month coincident peak method of demand allocation for Comm Ed instead of the 12-month coincident peak method advocated by the municipal customers. (672 F.2d at 82.) In addition, the court affirmed the Commission’s approval of a 100% demand ratchet, to apply during the system’s peak season, the four summer months. It found that “the ratchet approved by the Commission works in harmony with the 1-CP demand allocation method to distribute demand cost in an efficient and fair manner.” (672 F.2d at 84).¹

Finally, the court upheld the Commission’s finding that a price squeeze did not exist. The Commission had ruled that the 17% difference between the wholesale rate to the municipal customers and the relevant retail rate was justified. It based this finding on a comparative rate of return study which showed that Comm Ed earned a return of 7.95% on its service to the municipals and 8.41% on the relevant retail service. The court held that this was a valid means of testing for the existence of price squeeze.

7. Automatic adjustment clause, rate of return — *Louisiana Public Service Commission v. Federal Energy Regulatory Commission*, 688 F.2d 375 (5th Cir. 1982)

This case was concerned with rates set by the FERC for interstate sales of power among the four affiliated electric utilities of Middle South Utilities System. The Louisiana Public Service Commission sought review of two aspects of the FERC’s rate decision: (1) the expansion of the categories of expenses that could be recovered through the automatic adjustment formula, and (2) the allowance for rate of return on equity.

The court affirmed the FERC on both counts. As to the automatic adjustment clause, Middle South had sought and the Commission had approved the collection of operation, maintenance, and general and administrative expenses through the

¹The court upheld the Commission’s discretionary decision not to order refunds resulting from rejection of the company’s proposed 75% 23-month ratchet. (672 F.2d at 84-85).

clause. The Fifth Circuit ruled that automatic adjustment clauses are not restricted to the recovery of unstable, unpredictable expenses and accordingly affirmed the Commission decision. With respect to rate of return, the court approved the Commission's allowance of 14% on equity, rejecting the arguments of the Louisiana Commission that a traditional cost of capital analysis was inappropriate for the type of interaffiliate transactions at issue in the case.

8. Demand ratchet, stratified rate design — *The Second Taxing District of the City of Norwalk et al. v. Federal Energy Regulatory Commission*, 683 F.2d 477 (D.C. Cir. 1982)

Municipal customers of Connecticut Light and Power Company sought judicial review of the FERC decision approving a 100% billing demand ratchet for partial requirements customers of the company and adopting a "stratified" rate design by which different demand and energy charges are imposed for peak and off-peak usage. The court affirmed the Commission on both points. It found sufficient record support for the Commission's determination that the ratchet clause would prove useful in encouraging reductions in demand at the time of the system peak. In addition, it found that the ratchet will not redistribute demand costs unfairly, noting that partial requirements customers have the ability to utilize their own generating facilities in order to reduce their peak demand.

As to the stratified rate design, the court agreed with the Commission that the company had made an adequate showing that the peak/off-peak stratifications tracked actual costs of service.

9. Attrition allowance — *Southern California Edison Company v. Federal Energy Regulatory Commission*, 686 F.2d 43 (D.C. Cir. 1982)

In this appeal, Southern California Edison challenged, among other things, the Commission's rejection of its proposed attrition allowance without a hearing. In upholding the Commission, the court agreed with the Commission's conclusion that since Edison's attrition study had elevated the company's 1981 test year projected costs to the 1982 expense levels without the required cost data, the proposal contravened the applicable Commission regulations.

10. Undue Discrimination — *City of Frankfort, Indiana v. Federal Energy Regulatory Commission*, 678 F.2d 699 (7th Cir. 1982)

This case concerned allegations of discrimination among five municipal partial requirements customers of Public Service Company of Indiana. Four of these were offered and accepted fixed-rate contracts in the period from 1968 to March 1971. One of them, however, the City of Frankfort, did not agree to a contract with PSCI until some months later, by which time PSCI had a change of policy and insisted on a contract permitting unilateral rate increases. Frankfort alleged undue discrimination.

The court affirmed the Commission's holding that any rate disparity arising out of the contractual differences was justified by differences in facts — cost-of-service or otherwise. (678 F.2d at 706-7). In its view, the rate differential was justified by the good-faith change in PSCI's policy which discontinued the use of fixed rate contracts, combined with Frankfort's failure to execute a fixed-rate contract during the period when one was available.

11. Interconnection agreement — *Ohio Power Company v. Federal Energy Regulatory Commission*, 668 F.2d 880 (6th Cir. 1982)

The Sixth Circuit affirmed the FERC's approval of an amendment to the American Electric Power (AEP) interconnection agreement designed to increase the primary capacity equalization charge among the AEP companies. This charge fixes the rate at which the AEP companies purchase generating capacity from each other to supplement the capacity of their own systems. The court, in affirming the Commission, stressed that its approval of the proposed modification was but a pragmatic resolution of the problem, without prejudice "to the right of the petitioners to initiate new proceedings before the Commission for re-examination of Modification No. 3." (668 F.2d at 887).

IV. RULEMAKING PROCEEDINGS

In 1982, nearly all the final rules passed by the Commission involved procedural matters.² As part of the Reagan Administration's effort to eliminate unnecessary regulation, the Commission made a concerted effort to reduce filing requirements for electric utilities at FERC. The Commission:

— revised Form 1 (Annual Report of Electric Utilities) to eliminate unnecessary reporting requirements. Order No. 200, Docket No. RM80-55, issued January 6, 1982.

— extended the filing date by one year for cost of service information required under § 133 of PURPA. Order No. 231, Docket No. RM82-28, issued May 19, 1982.

— revised its regulations under the Uniform System of Accounts governing the retention of records by utilities, by explicitly defining the types of records to be retained and in some instances shortening the retention period. Order No. 258, Docket No. RM81-4, issued September 13, 1982.

— revised Form 423 (Monthly Report of Cost and Quality of Fuels for Electric Plants) by reducing the number of utilities required to file the form. Order No. 264, Docket No. RM82-4, issued October 5, 1982.

— eliminated Form 4 (Monthly Power Plant Report), Form 67 (Steam Electric Plant Air and Water Quality Control Data) and Form 5 (Electric Utility Monthly Statement), because the information collected under these forms is now collected by the Energy Information Administration of DOE. See Order No. 201, Docket No. RM82-9, issued January 7, 1982; Order No. 257, Docket No. RM82-40, issued August 31, 1982. Order No. 265, Docket No. RM83-4, issued November 22, 1982.

The Commission also attempted to expedite proceedings and make procedural rules more understandable. In the Order No. 225 series, Docket No. RM78-22, issued April 18, 1982,³ the Commission reorganized, revised and updated its Rules of Practice and Procedure. The final rule removed all general rules of practice and procedure from 18 CFR Part I and placed them in Part 385. It also provided various means of expediting cases set for hearing, including delegating to the Chief

²The Commission did deny rehearing and lift the stay of Order 144 involving tax normalization. Order No. 144-A, Docket No. RM80-42 *et al.*, issued February 22, 1982.

³Order No. 225-A, (Order Denying Rehearing, Clarifying Final Rule and Making Corrections to Final Rule) issued August 12, 1982; Order No. 225-B (Order Denying Petitions for Procedural Rulings), issued August 12, 1982; and Order No. 225 (Order Denying Petition for Stay on Final Rule), issued August 24, 1982.

Administrative Law Judge the authority to consolidate and serve and permitting a Presiding Administrative Law Judge to phase cases and to dispose summarily of issues or an entire proceeding without a hearing.

Several important rulemakings proposed in 1982 were still pending at the end of the year. The most significant was the generic rate of return rule proposed in a notice issued on August 26, 1982, in Docket No. RM80-36. The proposed rule would eliminate rate of return on common equity as a contested issue from individual electric utility rate cases. Instead, the Commission would divide jurisdictional companies into three risk classes, based on using one or more possible risk factors. It would then determine the average cost of equity for each of the three classes for a base year and this figure would be the allowed base period cost of equity for each company in the class. The generic return on equity for each class would be adjusted to maintain a constant risk differential with 10 year Treasury bonds — that is, the allowed return on equity would rise or fall along with Treasury bond yields.

Perhaps equally significant were two rulemakings in which the Commission proposed substantial filing fees for various applications. Specifically, the Commission proposed to implement a fee schedule for services regarding the filing of a (1) petition for a declaratory order, (2) request for interpretation by the Office of the Chief Accountant, (3) request for review of a DOE remedial order, and (4) request for review of a DOE denial of adjustment. (Docket No. RM82-35, issued June 24, 1982). The Commission also proposed a new fee schedule for rate schedule filings, corporate applications, applications for orders directing interconnection on wheeling, applications for certification of qualifying status and applications to issue securities. (Docket No. RM82-38, issued September 1, 1982). These proposals, which are still pending and have met with a great deal of opposition, were part of the policy of the Reagan Administration to insure that federal agencies be self sustaining to the fullest extent possible.

At the end of 1982, the following rulemaking dockets initiated before 1982 were still pending:

RM82-7	Qualifying facilities
RM81-40	FOI Request fees
RM81-38	CWIP in rate base
RM80-60	Revision of <i>ex parte</i> rules
RM79-80	Price squeeze substantive rules
RM79-79	Price squeeze procedural rules
RM79-52	Reporting capacity shortages (interim rule issued)
RM79-49	Cash working capital
RM79-28	§ 202(c) emergency rates
RM77-1	Return on equity [subsumed by RM80-36 but never terminated]

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