UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Inquiry Regarding the Commission's Policy for Determining Return on Equity	Docket No. PL19-4-000

INITAL COMMENTS OF PPL CORPORATION

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PPL Corporation ("PPL Corp." or "PPL") hereby submits initial comments on behalf of its domestic transmission owning subsidiaries, PPL Electric Utilities Corporation ("PPL EU") and Louisville Gas & Electric and Kentucky Utilities ("LGE/KU") (collectively, the "PPL Companies") in response to the Federal Energy Regulatory Commission's ("FERC" or "Commission") Notice of Inquiry Regarding the Commission's Transmission Policy on Determining Return on Equity ("NOI").[1]

I. INTRODUCTION

The PPL Companies invest a substantial amount of capital in their transmission assets. They do so fundamentally for the benefits of their wholesale and retail customers, but these investments have benefits for all users of the transmission system. When the PPL Companies invest in transmission, they tap a reserve of customer and political capital. Especially in the PPL EU transmission zone, PPL has experienced increasing opposition to its transmission projects. This opposition makes continued investment in customer reliability, resiliency of the system, and market efficiency more difficult. The increased opposition to transmission construction also makes investment in transmission far riskier than it was several years ago, all at a time when the

[1] *Inquiry Regarding the Commission's Policy for Determining Return on Equity*, Docket No. PL19-4, 166 FERC ¶ 61,207, Mar. 21, 2019 ("ROE NOI").

increased competition for investment (both internal and external) has grown. The PPL Companies are obligated to maintain a reliable transmission network to serve their customers and ensure the proper functioning of the power system. However, legal precedent from the Commission and the Courts also requires that they be appropriately compensated for the risks and challenges associated with maintaining that system.

Every time the PPL Companies invest in needed transmission infrastructure, they put PPL's brands, reputation, and image on the line. These investment risks should be reflected in the returns to transmission investment available to the PPL Companies, most importantly the return on equity ("ROE") issues open for comment in this notice of inquiry. Historically, FERC-regulated transmission investment has been competitive with other potential utility investments and FERC's ROEs have not disincentivized marginal investment in the transmission system. It is vital that the Commission retains its longstanding policies that ensure adequate returns reflecting the real risk and choices involved in investing in transmission.

PPL appreciates the opportunity to comment on the Commission's ROE policy. PPL seeks to ensure that ROEs continue to be structured to appropriately compensate utilities for the risks and challenges they face. PPL commends the Commission for its efforts in this regard and submits the following comments on select questions raised in the NOI.

II. BACKGROUND ON PPL CORPORATION AND THE PPL COMPANIES

PPL Corp., headquartered in Allentown, Pennsylvania, is a utility holding company, incorporated in 1994, in connection with the deregulation of electricity generation in Pennsylvania. PPL Corp. was founded to serve as the parent company to PPL EU, a regulated utility, and to generation and other unregulated business activities. PPL Corp., through its regulated utility subsidiaries, delivers electricity to customers in the United Kingdom, Pennsylvania, Kentucky, and Virginia; delivers natural gas to customers in Kentucky; and generates electricity from power plants in Kentucky.

PPL EU was founded in 1920 as Pennsylvania Power & Light Company. PPL EU is a Pennsylvania corporation and a wholly owned subsidiary of PPL Corp. PPL EU is a founding member of PJM Interconnection, LLC ("PJM"), and participates as an active member in the PJM transmission owner sector. PPL EU also distributes electricity to retail customers in its service territory in central and eastern Pennsylvania, and is a provider of last resort under Pennsylvania's Electricity Generation Customer Choice and Competition Act. PPL EU is a load-serving entity in PJM and is a signatory to the PJM Consolidated Transmission Owners Agreement, the PJM Operating Agreement, and the PJM Reliability Assurance Agreement.

LG&E and KU are both public utilities and are wholly owned subsidiaries of LG&E and KU Energy LLC, a public utility holding company and a wholly owned subsidiary of PPL Corp. LG&E is an electric and natural gas utility based in Louisville, Kentucky. LG&E currently serves customers in Louisville and sixteen surrounding counties. KU is an electric utility based in Lexington, Kentucky, serving seventy-seven Kentucky counties and five counties in Virginia (under the name Old Dominion Power Company). LG&E/KU provide open access transmission service pursuant to the terms and conditions of the LG&E/KU Open Access Transmission Tariff currently on file with the Commission.

III. DISCUSSION

Following the *Emera Maine* decision at the DC Circuit, FERC issued the *Coakley* and *MISO* Briefing Orders outlining several proposed changes in its longstanding methodology for addressing ROEs embedded in transmission rate proceedings. FERC also issued a Notice of Inquiry ("NOI") inviting comment on the newly proposed methodology changes, as well as a series of other questions related to ROEs:

A. Role and Objectives of the Commission's Base ROE Policy

1. General comments on proposed methodology (A1, A2)

The NOI begins with several high-level questions on ROE methodology:

> *A1. To what extent would the ROE methodology described in the Coakley and MISO Briefing Orders impact the predictability of ROE determinations and the costs for market participants of making or intervening in such proceedings?*
>
> *A2. How would using the ROE methodology described in the Coakley and MISO Briefing Orders affect an investor's ability to forecast the ROE the Commission would establish in a litigated proceeding and the ability of participants to propose, contest, and settle base ROEs as compared to using only the DCF methodology?*[2]

PPL responds to the proposed ROE methodology described in the *Coakley* Briefing Order in more detail in Section D, related to proxy groups, and Section G, related to the first prong of the § 206 analysis, below. On proxy groups, PPL believes the proposed methodology creates buckets that are too restrictive and fail to capture a true representation of the market. The proxy group rules should contemplate the reality of constantly shifting capital markets, and market conditions more generally. Accordingly, the Commission should enable proxy groups that reflect the real-world investment factors utilities face when competing for capital. Based on factors including the timing of the filing, the utility's geographic location, and the capital conditions the

[2] ROE NOI at P 31.

utility faces, these proxy groups may include non-utility companies, or utility companies with a broader range of credit profiles as appropriate.

For the first prong of the § 206 analysis, the "safe-harbors" defined under the Commission's proposed methodology are unnecessarily narrow. The *Emera Maine* decision allows for broader buckets than the quartiles proposed by the Commission.[3] Widening these buckets to thirds (or "tertiles") would be more consistent with prevailing law. PPL further proposes that the paradigm considering below- and above-average risk utilities differently from average risk utilities as part of the § 206 analysis is unnecessary and should be replaced by a simpler model that more accurately and reasonably reflects the real landscape for utilities.

2. Nationwide ROE (A3)

The Commission next asks whether it should impose a single ROE on the entire country:

> *A3. Currently, public utilities in different Independent System Operators (ISOs) or RTOs may receive different ROEs, despite all using national proxy groups, due primarily to differences in when FPA section 205 or 206 proceedings were initiated. Are such variations justified, and, if not, should the Commission consider applying the same ROE to all utilities in RTOs/ISOs based on the most recent proceeding?*[4]

PPL strongly opposes a national ROE for all utilities. Adopting a single ROE would effectively nationalize every rate proceeding, as every utility in the country would have an interest in the outcome given that it would reset the ROE for all utilities. This would create significant administrative burdens on the Commission and the industry. In addition to dramatically raising the stakes on rate cases, and inviting hundreds of intervenors, it would make individual rate management substantially more challenging. A utility's ROE could be expected to change multiple times, perhaps dozens of times, within a single rate year. Utilities would have

[3] *See Emera Maine v. F.E.R.C.*, 854 F.3d 9 (D.C. Cir. 2017).
[4] ROE NOI at P 31.

a difficult time budgeting, which would make their access to long-term capital more difficult. This would lead to confusion and frustration for customers, who could never predict expected rates with any level of precision.

Adopting a single national ROE would also be inconsistent with the Federal Power Act ("FPA"). The FPA allows individual utilities the right to set their own just and reasonable rates.[5] For FERC to change a utility's rate outside of a utility-initiated rate proceeding requires a showing that the existing rate is unjust and unreasonable under FPA § 206,[6] something it cannot do at the aggregate level.

3. Vintage ROEs (A4)

The Commission has requested comments on so-called "vintage" ROEs, where utilities would track separate ROEs for different transmission plant, depending on the year the plant was installed:

> *A4. Should the ROE reflect the cost of capital at the time of the investment or be subject to adjustment to reflect the contemporary ROE required by investors?*
>
> > *A4.a. Should the Commission consider a "vintage approach," with ROE fixed for the life of the asset at the time that each asset was completed?*
> >
> > *A4.b. Would such a "vintage approach" need to be coupled with an annual national default ROE for investments made in that year, so as to minimize the need for numerous annual litigated ROE proceedings for each public utility that made an investment during that year? What procedure should be used to determine such a default ROE?*

[5] *See* 16 U.S.C. § 824d(a) (§ 205) ("All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.").
[6] *See* 16 U.S.C. § 824e(a) (§ 206) ("Whenever the Commission . . . shall find that any rate . . . is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate . . .").

PPL opposes vintage ROEs as unnecessary and unmanageable and joins in comments to that effect submitted by EEI and the PJM Transmission Owners.[7] Using vintage ROEs would be extremely complex and ultimately add accounting costs to be paid by ratepayers with no tangible benefit. It would also change the relative attractiveness of transmission owning utilities to investors compared with distribution-only or integrated utilities when those utilities do not adopt vintage ROEs for their distribution assets. If the trend in ROEs is up, transmission would be less attractive to investors because transmission owning utilities would continue to carry the legacy low ROE vintages on their books. The opposite would be true if the ROE trend is down.

Moreover, vintage ROEs do not reflect the way in which utilities finance their transmission projects. Utilities often refinance their transmission projects several times over the life of the project and the ROEs should be able to reflect those changes. If the Commission decides to adopt vintage ROEs, they should only be applied at the option of the utility.

B. ROEs for Different Commission-Regulated Industries

PPL has no specific comments on whether the Commission should apply a single ROE policy across the electric, interstate natural gas and oil pipeline industries.

C. Performance of the DCF Model

PPL joins the comments of EEI and the PJM Transmission Owners to the extent they address the performance of the DCF model.

D. Proxy Groups

The Commission is responsible for determining the "risk-adjusted expected rate of return sufficient [for a utility] to attract investors."[8] Because many utilities are not publicly traded, this analysis must be done via "roundabout estimations, including relying on the ROEs of

[7] *See* Comments of the Edison Electric Institute, Docket No. PL19-4 ("EEI Comments") at 23–25; Comments of the PJM Transmission Owners, Docket No. PL19-4 ("PJM TO Comments") at 40.
[8] *S. California Edison Co. v. F.E.R.C.*, 717 F.3d 177, 179 (D.C. Cir. 2013), *citing Canadian Ass'n of Petroleum Producers v. F.E.R.C.*, 254 F.3d 289, 293 (D.C. Cir. 2001).

comparable publicly-traded companies, termed a proxy group."[9] By law, proxy groups must "make[] sense in terms of relative risk."[10] The returns should be "'commensurate with returns on investments in other enterprises having corresponding risks' and 'sufficient to assure confidence in the financial integrity of the enterprise . . . [and] maintain its credit and . . . attract capital.'"[11]

1. The Commission Should Expand Proxy Groups to Include Any Companies with Similar Credit Ratings to the Subject Utility (D1, D3).

Traditionally, FERC has limited proxy groups for electric utilities to those listed on *Value Line*'s electric utility group listing.[12] However, in the NOI, the Commission inquired about this long-held assumption in two relevant questions:

> *D1. Should proxy groups for electric utilities, as well as natural gas and oil pipelines, consist only of companies with corresponding regulated businesses?*
>
> *D3. Should the Commission consider non-energy companies when selecting proxy groups?*[13]

PPL suggests that the Commission should change its traditional practice of excluding non-electric utilities from proxy groups. Current Commission policy limits proxy group composition to electric companies within one credit notch up or down of the subject utility. As noted by other commenters, due to consolidation of the electric industry, this policy has created concerns about a lack of a comparison group of adequate size to ensure a representative proxy

[9] *S. California Edison*, 717 F.3d at 179, *citing Pub. Serv. Comm'n of Ky. v. F.E.R.C.*, 397 F.3d 1004, 1006–07 (D.C. Cir. 2005).
[10] *Petal Gas Storage, L.L.C. v. F.E.R.C.*, 496 F.3d 695, 700 (D.C. Cir. 2007).
[11] *Id.*, *citing Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) (internal citations omitted).
[12] *See Martha Coakley v. Bangor Hydro-Electric, et al.*, Opinion No. 531, Order on Initial Decision ("Opinion 531"), 147 FERC ¶ 61,234, Jun. 19, 2014, at P 100 (affirming "use of *Value Line* data as a proxy group screen"); *S. Cal. Edison*, 131 FERC ¶ 61,020 at P 51 (accepting *Value Line* electric utility "screening criteria without further discussion").
[13] ROE NOI at P 34.

group.[14] The risk is that proxy groups are overly constrained so as to not reflect appropriate comparative risk.[15]

Further, investors have a full menu of options when evaluating where to invest their money and do not view electric utilities in a vacuum. Rather, all industries compete for the same capital, irrespective of the regulatory environment in which they operate.[16] Utilities offering regulated returns must compete for capital with unregulated businesses frequently able to provide higher returns. In setting the rules for constructing the proxy groups that inform these regulated returns, the Commission should consider the effects of competition for capital and broaden its economic outlook beyond the utility industry.

The Commission should adopt a flexible policy that allows utilities to propose proxy groups composed of companies in any industry with credit ratings one notch above or below that of the subject utility.[17] Intervenors challenging utility rates under § 206 of the FPA should be given similar flexibility in their proposed proxy groups. This alleviates the sizing concerns while retaining parameters that ensure that the proxy group presents an accurate representation of market conditions and a utility's risk profile. The Commission should evaluate such proxy groups on a case-by-case basis based on the market conditions existing at the time of the proceeding. It should allow non-utility proxies with similar credit ratings if there is evidence that excluding non-utility companies would paint an incomplete picture of the capital market conditions. Importantly, this proposal retains the principle of comparable risk, where the

[14] *See* EEI Comments at 25–26; *see also* PJM TO Comments at 44–45.
[15] *See Petal Gas*, 496 F.3d at 700.
[16] *See* EEI Comments at 28.
[17] This is consistent with the FPA so long as the rates developed from the proposed proxy groups are "just and reasonable." *See* FPA § 205(a).

Commission has found that entities whose returns are commensurate with those of the subject utility should be eligible for inclusion in the proxy group.[18]

Current limitations in existing policy related to proxy group composition could result in electric utility ROEs lower than those of companies in other industries with similar risk profiles. Such a result will deter investment and create challenges to meeting FERC's overarching goal of promoting a robust, reliable transmission system. The adoption of policies that allow proxy group composition on a case-by-case basis to reflect current market conditions and take into consideration industries with similar risk profiles will produce proxy groups that more accurately reflect the range of data evaluated by investors when making investment choices.

2. The Commission Should Consider Proxy Groups of Electric Utilities Within Two Notches of the Subject Utility's Credit Rating (D6).

Regardless of whether the Commission expands consideration of proxy groups to include non-utilities with similar credit ratings to the subject utility, it should consider proxy groups of electric utilities within two notches of the subject utility's credit rating. This is contemplated in an NOI question about modifying the credit rating screen:

> *D6. What would be the impact of the Commission modifying the credit rating screen to include all investment-grade utilities in the proxy group?*[19]

As discussed above, there is growing concern that consolidation in the industry will lead to difficulty crafting "large, representative comparison group[s]" eligible for consideration in electric utility proxy groups.[20] One option for addressing this concern is to allow proxy groups beyond electric utilities as discussed above. A second option, endorsed by other commenters, is

[18] *See Petal Gas*, 496 F.3d at 700, *citing Hope*, 320 U.S. at 603.
[19] ROE NOI at P 34.
[20] *See* PJM TO Comments at 44–45; *see also* EEI Comments at 25–26.

to expand the window of electric utilities eligible for consideration in the proxy group.[21] PPL proposes to expand the credit rating screen to include utilities two notches above and below the subject utility. Two credit notches would be sufficient to capture the vast majority of investment grade utilities, while retaining a sufficient credit rating screen to exclude companies with extreme risk profiles (high or low) that are not representative of the industry.[22]

3. The Commission Should Relax the M&A Activity Screen to Evaluate the Magnitude of the M&A Effect (D8).

Similarly, concerns about industry consolidation leading to insufficiently sized proxy groups have prompted renewed focus on the M&A activity screen.[23] The Commission's practice has been "to eliminate from the proxy group any company engaged in M&A activity significant enough to distort the DCF inputs."[24] According to the Commission, "large scale [M&A] activity can distort share prices by creating uncertainty (positive and negative) about the impact of change" and M&A "transactions can also influence the stability of the dividend pattern."[25] The Commission has also recognized "another reason for caution:"

> [O]nce a company is the subject of an acquisition, the growth rate is based on whatever is expected to happen between that time and when the buyout is completed, which is inconsistent with the Commission's method which seeks to compute a growth rate beyond five years.[26]

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[21] *See* PJM TO Comments at 45.
[22] *See id.*, *citing Tallgrass Transmission, LLC*, 125 FERC ¶ 61,248 at P 77, n.79 (2008).
[23] *See* EEI Comments at 25–27.
[24] Opinion 531 at P. 114; *see also*, *Atl. Grid Operations A LLC*, 135 FERC ¶ 61,144, May 19, 2011, at P 88 n.55; *RITELine Ill., LLC*, Order on Transmission Rate Incentives and Formula Rate Proposal, 137 FERC ¶ 61,039, Oct. 14, 2011, at P 68.
[25] *Kern River*, Order on Rehearing, Proposed Settlement and Paper Hearing, Opinion No. 486-B, 126 FERC ¶ 61,034, Jan. 15, 2009, at P 79.
[26] *Id.*, *quoting Enbridge Pipelines (KPC)*, Order on Initial Decision, 100 FERC ¶ 61,260, Sep. 10, 2002, at P 237.

However, the Commission has never considered this policy an absolute. When utilities present evidence that an anticipated merger is not distorting stock prices, the Commission has allowed the company expecting a merger to be retained in the proxy group.[27]

The Commission's NOI invited comments on the continued use of the M&A activity screen:

> *D8. The Commission excludes from the proxy group companies with merger activity during the six-month study period that is significant enough to distort study inputs. Should the Commission continue using our existing merger screen?*
>
> > *D8.a. If so, should the Commission revise its standards for what conduct constitutes merger and acquisition activity?*[28]

PPL submits that only companies with *significant* M&A activity should be excluded from the proxy group. The test proposed by EEI that limiting M&A activity to a relatively small (5–10% of market capitalization) portion of the proxy group is more than sufficient to protect from these anomalous conditions affecting the results of the analysis.[29] PPL also agrees with EEI that even if this *de minimis* threshold is exceeded, the Commission should evaluate whether there is actually any appreciable impact on the stock prices of the companies that may have been otherwise excluded from the proxy group.[30]

4. Measure of Central Tendency (D10)

In the *Coakley* Briefing Order, the Commission proposed a methodology of determining the central tendency of the zone of reasonableness to determine an estimated cost of equity for

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[27] *See, e.g.*, *Bangor Hydro-Elec. Co.*, Initial Decision, 111 FERC ¶ 63,048, May 27, 2005, at PP 67–68 (allowing utilities with a pending proposed merger to be retained in the proxy group), *aff'd in relevant part*, *Bangor Hydro-Elec. Co.*, Opinion No. 489, 117 FERC ¶ 61,129, Oct. 31, 2006, at P 67 (agreeing with inclusion given evidence that merger had no impact on financial data of proxy group companies).
[28] ROE NOI at P 34.
[29] *See* EEI Comments at 26–27.
[30] *See id.*

average risk utilities.[31] The Commission announced that it intended to formalize a bifurcation of utility companies based on whether they had single utility ROEs, or shared ROEs with a larger RTO or ISO group (as do, for example, the NE-ISO and MISO utilities).[32] This policy cites a 2010 *Southern California Edison* decision, where the Commission determined that because "the median places more weight on the middle values of a range of values than does the midpoint . . . it potentially produces a value that is not appropriate for a diverse group of utilities."[33] Utilities with their own unique ROEs would continue to use the "best measure of central tendency," the median.[34]

In the Notice of Inquiry, the Commission invites comments on this policy of splitting utilities into two groups based on whether they share ROEs with other utilities in an RTO or ISO:

> *D10. The Commission currently uses midpoints to determine the central tendency of the zone of reasonableness when determining RTO-wide ROEs. Should the Commission adopt a policy of using medians for this purpose?*
>
> > *D10.a. Would the use of multiple ROE methodologies, as proposed in the Coakley Briefing Order, undercut the Commission's current rationale for using the midpoint in RTO-wide base ROE?*
> >
> > *D10.b. Should the size of the proxy group be considered in this decision?*[35]

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[31] *Martha Coakley v. Bangor Hydro-Elec. Co.* ("*Coakley* Briefing Order"), 165 FERC ¶ 61,030 (2018) at P 17.

[32] *Id.* at n. 46 (announcing "[t]he Commission will continue to use the midpoint of the zone of reasonableness as the appropriate measure of central tendency for a diverse group of average risk utilities and the median as the measure of central tendency for a single utility").

[33] *S. Cal. Edison Co.*, Order on Paper Hearing and Request for Rehearing, 131 FERC ¶ 61,020, Apr. 15, 2010, at P 91, *remanded on other grounds sub nom. S. Cal. Edison Co. v. F.E.R.C.*, 717 F.3d 177, 183–87 (D.C. Cir. 2013).

[34] *Id.* at PP 91–92 (adding that the median, rather than the midpoint, is the "most refined measure of central tendency").

[35] ROE NOI at P 34.

PPL echoes the comments of EEI and the PJM Transmission Owners that the Commission should not bifurcate the measurement of central tendency for electric utilities based only on whether they share ROEs with fellow RTO or ISO members.[36]

Utilities face similar comparative risks regardless of whether they retain the right to propose unique ROEs. It would be discriminatory to treat utilities different based solely on whether they share ROEs with other utilities. Accordingly, the Commission should adopt a policy that allows use of the midpoint to determine the measure of central tendency in all cases, or at least in all cases for transmission owning utilities in an RTO or ISO. As explained in the PJM Transmission Owner Comments, such utilities "share common obligations and risks arising from their participation in the RTO" and the range of proxy group ROEs "fairly brackets the range of reasonableness for all transmission owners in the RTO, whether the issue concerns a single ROE for all of them or an ROE for just one of them."[37] PPL agrees that there is no justification for separating RTO/ISO members with unique ROEs from those sharing ROEs in this analysis. If midpoint is just and reasonable for the latter, is should also be just and reasonable for the former.

E. Financial Model Choice

PPL joins the comments of EEI and the PJM Transmission Owners to the extent they address financial model choice.

F. Mismatch Between Market-Based ROE Determinations and Book-Value Rate Base

PPL joins the comments of EEI and the PJM Transmission Owners to the extent they address the mismatch between market-based ROE determinations and book-value rate base.

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[36] *See* PJM TO Comments at 41–44, EEI Comments at 22.
[37] PJM TO Comments at 43.

G. First Prong of ROE Determination

In the *Coakley* Briefing Order, the Commission defined a new methodology for identifying the range of presumptively just and reasonable ROEs to use in assessing a challenge under the first prong of § 206. This methodology utilized the "three financial models that produce zones of reasonableness—the DCF, CAPM, and Expected Earnings models—to establish a composite zone of reasonableness."[38] It then used "that composite zone of reasonableness . . . to identify a range of presumptively just and reasonable ROEs for utilities with a similar risk profile to the targeted utility."[39] PPL joins EEI and the PJM Transmission Owners in approving of this general methodology.[40]

However, the *Coakley* Briefing Order then went on to define three categories of utilities based on risk profile, labeling them below-average, average, and above-average.[41] Each category was assigned a zone of reasonableness quartile, within which its ROE will be deemed presumptively just and reasonable.[42] The fourth quartile was divided in half, assigned to the high and low ends, and excluded from the analysis.[43] The Commission's NOI invited comments on this element of the methodology:

> *G1. How should the Commission determine if existing ROEs are just and reasonable?*
>
> *G2. Is the quartile approach that the Commission proposed in the Coakley and MISO Briefing Orders appropriate? If not, how should the Commission revise this methodology?*[44]

PPL proposes changes to two elements of the quartile approach outlined in the *Coakley* Briefing Order. First, PPL joins with the PJM Transmission Owners in proposing the use of a

[38] *Coakley* Briefing Order at P 16.
[39] *Id.*
[40] *See* EEI Comments at 7–9; PJM TO Comments at 9.
[41] *Coakley* Briefing Order at P 27.
[42] *Id.* at PP 26–27.
[43] *Coakley* Briefing Order at P 27.
[44] ROE NOI at P 37.

broader range than quartiles such as thirds (or "tertiles") to capture the respective zones of reasonableness. PPL proposes two possible methodologies using thirds. Second, PPL suggests that the Commission should revisit its paradigm of dividing utilities into below-average, average, and above-average risk. The vast majority of utilities are likely to be considered average risk in most cases and outliers should be addressed utilizing other tools, such as incentives.

1. Quartile Approach (G1, G2)

In *Emera Maine,* the Court emphasized that § 206 analysis does not allow the Commission to overturn an existing rate simply because a different rate would be just and reasonable if filed as a new rate under § 205. Instead, a utility is presumptively safe from challenge if its rate falls within a "broad range of potentially reasonable ROEs."[45] Indeed, the Court emphasized three times that the range must be "broad," citing Supreme Court precedent on this exact point.[46]

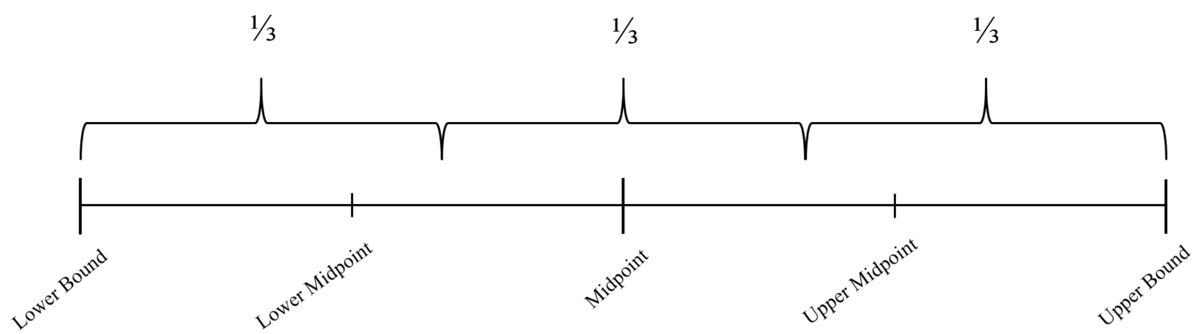
PPL joins with the PJM Transmission Owners in suggesting that the quartile approach proposed in the *Coakley* Briefing Order is too narrow to be consistent with this longstanding precedent.[47] As the PJM Transmission Owners point out, the analysis suggests that although referring to quartiles, the proposal in the *Coakley* Briefing Order really divides the world into thirds using the below-average / average / above-average risk utility paradigm.[48] The proposal in the *Coakley* Briefing Order also removes the lowest and highest eighths, which shifts the

[45] *Emera Maine*, 854 F.3d at 21, *citing Panhandle E. Pipe Line Co. v. F.E.R.C.*, 777 F.2d 739, 746–47 (D.C. Cir. 1985).
[46] *Emera Maine*, 854 F.3d at 23, *citing F.E.R.C. v. Conway Corp.*, 426 U.S. 271, 278 (1976) (approving FERC's recognition of "considerable latitude within the zone of reasonableness"); *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 770 (1968) (recognizing a "broad zone of reasonableness" in ratemaking).
[47] *See* PJM TO Comments at 9–12.
[48] *See id.* at 10.

remaining quartiles to focus them on the respective midpoints.[49] The result is inconsistent with the intent to establish a broad range of potentially reasonable ROEs.[50]

There is a better way. As outlined in more detail in the PJM Transmission Owner Comments, the Commission could simply divide the range of ROEs into thirds and assign an average risk utility the middle third:[51]

FIGURE 1 – "Straight Thirds"



PPL believes such a methodology provides a more reasonable approach than the quartile approach proposed in the *Coakley* Briefing Order. If the Commission is concerned about the inclusion of outliers in the below- and above-average risk utility buckets, as can perhaps be assumed by the methodology proposed in the *Coakley* Briefing Order, there are ways to address that concern other than merely lopping these ranges off. Retaining the middle third for average-risk utilities, but creating overlapping thirds for the (likely rare) below- and above-average risk utilities would meet this goal without unnecessarily narrowing the range of presumptively just and reasonable ROEs:

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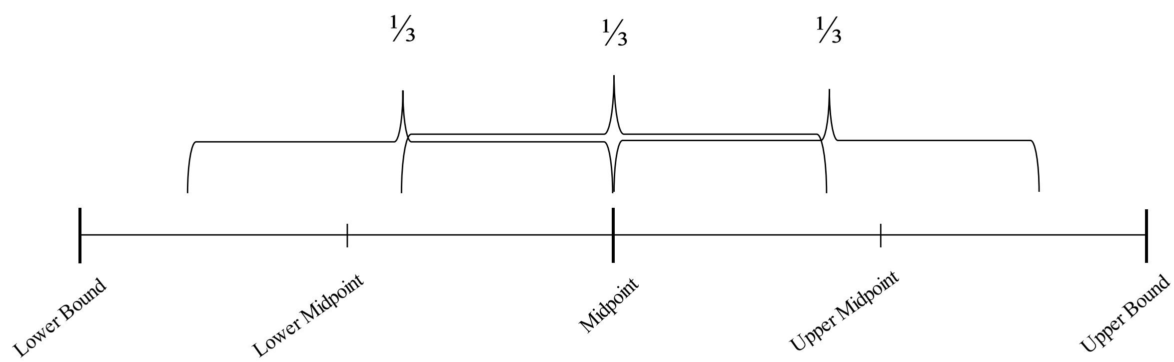
[49] *Coakley* Briefing Order at P 27.
[50] *See, e.g.*, *Emera Maine*, 854 F.3d at 27.
[51] *See* PJM TO Comments at 12.

FIGURE 2 – "Overlapping Thirds"



PPL also believes that this overlapping approach is consistent with the realities that capital markets face. The range of risks faced by average-risk companies, including average-risk utilities, overlap with the risks faced by below-average and above-average risk companies. As a result, the range of risks faced by such companies is not so easily segregated as the *Coakley* Briefing Order suggests. An approach that captures the overlapping risk ranges better reflects realities of the market.

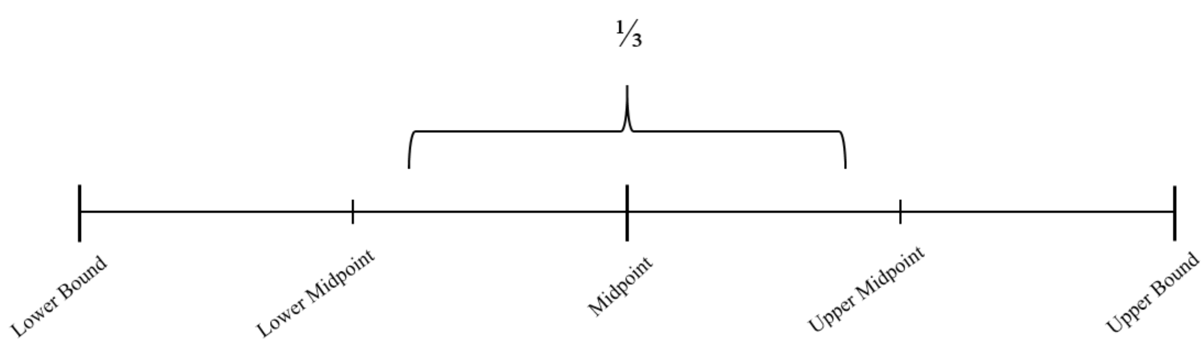
PPL does not disagree with the use of bands around a central tendency to determine a range of presumptively just and reasonable ROEs. However, narrowing three ranges to quartiles and excluding the high and low eighths is unnecessarily complex and produces a constrained range of reasonableness for an average risk utility. Because most utilities fall within the center band as average-risk, PPL believes that a less complex approach would also be more reasonable and consistent with legal precedent. PPL suggests a simple division of the composite results of the DCF, CAPM and Estimated Earnings models by three, resulting in groups of equal thirds with the point of central tendency falling within the middle third. These thirds can fill the entire range, or overlap to exclude outliers, so long as the Commission provides sufficient justification for its decision.

2. Below-Average / Average / Above-Average Risk Utility Paradigm (G1, G2)

Although PPL joins the PJM Transmission Owner comments in full, and supports the use of thirds rather than quartiles to determine the range of presumptively just and reasonable ROEs for the first prong of § 206, PPL would go a step further. PPL submits that because the vast majority of electric utilities are likely to fall within the group of "average risk" utilities for § 206 purposes, the methodology selected by the Commission should not rely on an overly detailed analysis in an attempt to incorporate above- or below-average risk utilities. There are easier ways to address those rare cases.

The methodology outlined in the *Coakley* Briefing Order can be improved simply by recognizing the fact that most utilities are—and should be—considered average risk. PPL proposes that the best methodology for the first prong of the § 206 analysis, and the one most consistent with the instruction of the *Emera Maine* Court, is simply to create a 1/3 range around the midpoint of the ROE proxy group. Any ROE within that range, regardless of the utility's relative risk profile, should be considered presumptively just and reasonable:

FIGURE 3 – "Middle Third Only"



If the Commission is concerned that this analysis will result in ROEs too low to reward above-average risk utilities who assume additional risk by furthering the public interest—for example by investing capital in high-risk projects to connect renewable energy, rather than by taking on unnecessary debt or simply through poor management—there are other ways to address this concern. For example, transmission incentives, mandated by Congress in the 2005 Energy Policy Act, and the subject of a separate NOI proceeding at Docket No. PL19-13, would be more than sufficient to compensate above-average risk utilities for assuming risks in the public interest.

H. Model Mechanics and Implementation

PPL joins the comments of EEI and the PJM Transmission Owners to the extent they address model mechanics and implementation.

IV. CONCLUSION

PPL appreciates the opportunity to comment on the important ROE issues raised in the NOI and thanks the Commission for raising this important topic.

Respectfully submitted,

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