

**UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION**

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

**INITIAL COMMENTS
OF THE
RESALE POWER GROUP OF IOWA**

Pursuant to the Notice of Inquiry (“NOI”) issued by the Federal Energy Regulatory Commission (“Commission” or “FERC”) on March 21, 2019,¹ the Resale Power Group of Iowa (“RPGI”) respectfully submits initial comments on whether, and if so how, the Commission should modify its policies concerning the determination of the base Return on Equity (“ROE”) to be used in designing jurisdictional rates charged by public utilities. RPGI is a party in two complaint proceedings pending before the Commission in which it has submitted extensive comments on these questions based on each case’s evidentiary record.² RPGI hereby incorporates those comments into this filing by reference as applicable and respectfully offers the following comments.

¹ *Inquiry Regarding the Commission’s Policy for Determining Return on Equity*, Notice of Inquiry, 166 FERC ¶61,207 (2019).

² See *Association of Businesses Advocating for Tariff Reform v. Midcontinent Indep. Sys. Operator, Inc.*, Docket No. 14-12-003, Initial Supplemental Brief of the Resale Power Group of Iowa, FERC Accession No. 201902013-5107 (filed February 13, 2019) and Supplemental Reply Brief of the Resale Power Group of Iowa, FERC Accession No. 20190410-5094 (filed April 10, 2019). See also *Arkansas Elec. Coop. Corp. v. ALLETE, Inc.*, Docket No. EL15-45-000, Initial Supplemental Brief of the Resale Power Group of Iowa (“RPGI EL15-45 Supp. Init. Br.”) FERC Accession No. 201902013-5139 (filed February 13, 2019) and Supplemental Reply Brief of the Resale Power Group of Iowa, FERC Accession No. 20190410-5095 (filed April 10, 2019).

RPGI'S INTEREST IN THIS PROCEEDING

RPGI is a special-purpose governmental entity organized in 1986 pursuant to Iowa law to purchase electric supply, transmission, and related services as an agent for its members. RPGI's members are 24 Iowa municipal utilities, one cooperative, and one privately-owned utility that (with one exception)³ are exempt from the Commission's jurisdiction under Section 201(f) of the Federal Power Act.⁴ A list of RPGI's members is contained in Attachment A. RPGI is legally separate and fiscally independent from other state and local governmental entities.

Virtually all of RPGI's members receive transmission service from ITC Midwest LLC pursuant to a formula rate set forth in Attachment O of the Open Access Transmission Tariff for the Midcontinent Independent System Operator. The base ROE for the MISO transmission owners is a component of this formula rate.

COMMUNICATIONS

The names, addresses and telephone numbers of the persons to whom communications concerning this matter should be addressed are as follows:

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³ The Amana Society Service Company is a small transmission-dependent electric utility that is privately owned by the Amana Society and provides service only to retail customers within the Amana Society in Iowa. Its current annual sales are 96,000 MWh and its peak load is 17 MW. Because of its size, it is not subject to rate regulation by the Iowa Utilities Board.

⁴ 16 U.S.C § 824(f).

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RPGI respectfully requests waiver of Rule 203(b)(3)⁵ to permit inclusion of the additional persons on the Commission's service list.

GENERAL COMMENT

THERE IS NO COMPELLING REASON FOR THE COMMISSION TO REVISE ITS LONG-STANDING RELIANCE ON THE DISCOUNTED CASH FLOW METHODOLOGY FOR SETTING RETURN ON EQUITY ALLOWANCES

1. *The Emera Maine court did not require the Commission to revamp its ROE-setting methodology.* For over twenty years, the Commission has preferred the Discounted Cash Flow ("DCF") methodology for setting electric utility ROEs and has refined its application of that methodology through many cases under many different financial market conditions.⁶ Until its adoption of Opinion No. 531, the Commission had not questioned the DCF model's fundamental efficacy, even in the immediate wake of the Great Recession of 2008-2009.⁷ Even in Opinion No. 531, the Commission did not abandon the DCF methodology's preferred status,

⁵ 18 C.F.R. §385.203(b)(3) (2019).

⁶ The NOI cites a number of cases in which the Commission fine-tuned the DCF method's variables to reflect changing market conditions. *See* NOI, 166 FERC ¶61,207 at ¶¶7-12.

⁷ In *Portland Natural Gas Transmission System*, Opinion No. 510-A, 142 FERC ¶ 61,198 at PP 219-220 (2013) (*aff'g in relevant part, Portland Natural Gas Transmission System*, Opinion No. 510, 134 FERC ¶ 61,129 (2011)), the top of the zone of reasonableness was 12.18% to 14.89% based on DCF results for a six-month period ended April 30, 2009, producing a median of 12.99%. In this company's next rate case, the DCF zone of reasonableness had declined to 8.69% to 11.59% based on DCF results for a six-month period ended November 30, 2010. *Portland Natural Gas Transmission System*, Opinion No. 524, 142 FERC ¶61,197 at PP 6, 290, and 323 (2013).

but rather used other methodologies as a check to determine placement of the ROE in the DCF zone of reasonableness.⁸

The court in *Emera Maine* did not question either the Commission's continued use of the DCF method or its reliance on other methodologies to inform ROE placement. Rather, it sought an explanation as to what evidence supported setting the ROE at the upper midpoint, if (as the Commission found) the midpoint of the DCF zone of reasonableness represented the ROE for electric utilities of average risk and New England utilities were of average risk.⁹ According to the court, the Commission could reach the same result as long as it explained how it arrived at that result based on the evidentiary record¹⁰ - a measured course of action the Commission clearly understood was available to it, as evidenced by the MISO Briefing Order, but apparently did not choose to take.¹¹ Instead, the Commission has elected to respond to *Emera Maine* by proposing to upend decades of industry experience and caselaw, stripping away the DCF's preference, and unnecessarily compounding the complexity of ROE determinations.

The Commission's rationale to justify the NOI's proposed ROE methodology is far too insubstantial to support such a sweeping endeavor. In Opinion No. 531, the Commission justified its departure from placing the ROE for the New England Transmission Owners at the midpoint of the DCF zone of reasonableness by citing unprecedented market conditions that caused it to

⁸ *Coakley v. Bangor Hydro-Elec. Co.*, Opinion No. 531, 147 FERC ¶61,234, *order on paper hearing*, 149 FERC ¶61,032 (2014), *order on reh'g*, 150 FERC ¶61,165 (2015).

⁹ *Emera Maine*, 854 F.3d at 30.

¹⁰ *Id.*

¹¹ *Association of Businesses Advocating Tariff Equity v. MISO*, 165 FERC ¶61,118 at P 11 (2018) ("MISO Briefing Order") ("The D.C. Circuit vacated the Commission's determinations in Opinion No. 531, upon which the Commission relied extensively in its order on the First MISO Complaint (i.e. Opinion No. 551), meaning that Opinion No. 531 is no longer precedential, *even though the Commission remains free to re-adopt those determinations on remand as long as it provides a reasoned basis for doing so.*") (emphasis added; footnotes omitted).

doubt that the midpoint reflected a return sufficient to attract investors.¹² With market conditions now much more normal than those that the Commission labeled as “anomalous,” Opinion No. 531’s justification of the Commission’s very limited departure from the DCF method has fallen away.

Therefore, in the MISO Briefing Order, the Commission was required to articulate a new rationale. Referring to its briefing order in the New England ROE cases, the Commission stated:

[E]vidence indicates that investors do not rely on any one model to the exclusion of others. Therefore, relying on multiple financial models makes it more likely that our decision will accurately reflect how investors make their investment decisions.¹³

The NOI echoes this reasoning.¹⁴

This rationale is an exceedingly slender thread upon which to hang a wholesale revision of the Commission’s ROE setting methodology. First and foremost, it does not respond to the legal defect identified by the *Emera Maine* court. It may be true that investors use many tools for deciding how to invest their money and there may be evidence in the *Emera Maine* record to support that assertion. The statement, however, is beside the point. Considering the results of multiple ROE methodologies is exactly what the Commission did in Opinion No. 531 and the court did not find fault with the Commission doing so. Investors’ alleged reliance on multiple models does not justify changing the Commission’s longstanding commitment to, and reliance upon, the DCF methodology.

Second, while investors may rely on multiple models, RPGI is not aware of any investor that averages the results of multiple models in its decision making and there is no indication that averaging makes the ROE-setting process any more accurate than utilizing one method. The

¹² Opinion No. 531, 147 FERC ¶61,234 at P 145.

¹³ MISO Briefing Order, 165 FERC ¶61,118 at P 12.

¹⁴ NOI, 166 FERC ¶61,207 at P 24.

Commission claims that it intends to give equal weight to each model's results,¹⁵ but if a model produces a result that is significantly higher or lower than the results produced by other models, that result should trigger a review or detailed analysis of the reasonableness of that particular model's results rather than an averaging of the result with the others.

In short, the question is whether an ROE produced by averaging the results of multiple models more accurately reflects the cost of capital required by investors, given that all models have limitations and flaws or does it simply compound the those limitations and flaws and produce an ROE that bears little or no relationship to the actual cost of equity capital?¹⁶ RPGI submits that averaging the results of four models does not guarantee any greater level of accuracy than consistently relying on the results of a single model. If the Commission's goal is to enhance the accuracy of the ROE-setting process, the NOI's proposed methodology does not represent any reasonable progress to getting there.

The Commission's "new" rationale for departing from the DCF preference suffers from other flaws that RPGI identified in the briefs it submitted in response to the MISO Briefing Order. The bottom line, however, is this: totally revamping the Commission's long-standing DCF preference is completely unnecessary as a response to *Emera Maine* and, in fact, may create more legal issues than it resolves.

2. Current market conditions do not require replacing the Commission's DCF preference. The Commission's preference for the DCF method in setting ROE allowances has brought predictability and comparability to its determination of utility rates for many years. Not until its issuance of Opinion No. 531 did the Commission express any doubts about the DCF's

¹⁵ *Id.* at P 25.

¹⁶ For a discussion of the limitations and flaws in the Capital Asset Pricing Model, the Risk Premium Model, and the Expected Earnings Model, *see* RPGI EL15-45 Supp. Init. Br., pp. 30-41.

efficacy as a rate-making tool. Even then, the Commission did not identify any intrinsic defect in the DCF model itself but rather stated that it was “concerned that capital market conditions in the record are anomalous” and therefore indirectly impacting the model’s dividend yield and the growth rate inputs.¹⁷ Market conditions during a specific time period, not the DCF’s theoretical underpinnings, triggered the Commission’s consideration of alternate methodologies. In its brief in *Emera Maine*, the Commission advocated for the court to uphold Opinion No. 531 by arguing that financial conditions during the applicable test periods were “unique,” “unusual,” and “outside the normal range.”¹⁸

The six-month test period in *Emera Maine* ended over six years ago on March 31, 2013. Whether one accepts or rejects the Commission’s characterization of market conditions in *Emera Maine* and other ROE cases as anomalous, it is indisputable that current market conditions are more normal than they were earlier when those cases were litigated. If there were ever any reason to doubt the DCF’s results based on “anomalous market conditions,” that reason has surely passed.

The DCF methodology has been a reliable tool that has served the Commission well. The Commission should continue its preference for that model.

RESPONSE TO SPECIFIC NOI QUESTION

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?

Increasing the number of models used in setting ROEs as contemplated by the NOI would have a significant adverse impact on the participation of customer-aligned interests in rate

¹⁷ Opinion No. 531, 147 FERC ¶61,234 at P 145.

¹⁸ Brief of Respondent Federal Energy Regulatory Commission filed in *Emera Maine v. FERC*, D.C. Cir. Case No. 15-1118 et al. filed April 26, 2016, at 42 - 44.

proceedings before the Commission. Before discarding its longstanding DCF preference, the Commission should carefully weigh the unproved, highly speculative benefit of increased accuracy in ROE determinations against the potential loss of customer group participation. RPGI submits that the Commission's need for customer participation in its proceedings far outweighs the ephemeral benefits of the NOI's proposed methodology.

Predictability is quite valuable for groups like RPGI. The Commission's honing of the DCF methodology over the years has meant that the issues to be disputed in a rate proceeding involve exercises of judgment rather than methodology for which expert testimony is best suited. Experts for transmission owners have criticized this "mechanical" application of the DCF but before casting such predictability to the side, the Commission should recognize that narrowing the issues saves litigation costs for all parties which, even for utilities, ultimately translates to customer savings and leads to final, non-appealable outcomes much sooner.

This latter point deserves emphasis. While haste toward a definitive conclusion has not characterized the current round of ROE cases,¹⁹ reducing regulatory uncertainty nevertheless has tremendous value for all stakeholders in the rate-setting process. For customers like RPGI and its members, definitive rates permit budgetary planning. Less uncertainty (i.e. more predictability) also leads to better cost/benefit evaluations when deciding whether to participate in a given FERC proceeding. Substantial regulatory uncertainty requires incurring high costs for experts and trial counsel, which, for small consumer groups like RPGI, can effectively limit or bar them altogether from participation in Commission proceedings.

The NOI's proposed methodology would *increase* uncertainty by introducing a multitude of potentially disputable methodological issues into every ROE setting case, beginning with any

¹⁹ The complaint in *Coakley v. Bangor Hydro Elec. Co.*, Docket No. EL11-66, was filed on September 30, 2011.

order the Commission issues on remand in *Emera Maine* or any action it takes in response to NOI comments. Regulatory uncertainty could continue for years as parties on all sides with large amounts at stake exhaust their administrative rights before the Commission and inevitably seek judicial review. Prolonging this process by putting in place an untried methodology is not in anyone's best interest and certainly does not represent the optimal balancing of customer and investor interests.

If this process were inextricably entwined with achievement of a compelling policy objective, the prolonged uncertainty might be worth the potential public good that could be achieved. Here, however, there is no such objective and therefore little, if anything, to be gained by upending a long-established regulatory tool.

Moreover, the DCF model has never been shown to be irredeemably flawed and the Commission's preference for that model has never been shown to be unreasonable.²⁰ The DCF model is not broken and there is no reason to "fix" it, especially by adopting a methodology

²⁰ See A CUSTOMER COALITION RESPONSE TO THE EDISON ELECTRIC INSTITUTES WHITEPAPER ON THE FEDERAL ENERGY REGULATORY COMMISSION'S TWO-STEP DCF METHODOLOGY FOR CALCULATING ALLOWED RETURNS ON EQUITY (2018) available at <https://www.nasuca.org/nwp/wp-content/uploads/2018/06/Final-Customer-Coalition-Whitepaper-Response.pdf> (last viewed June 24, 2019) p. 13 ("In the absence of any direct measure of the equity return required by a prospective investor in a public utility company, the Commission's DCF method produces reasonable estimates that appropriately reflect changing market conditions and expectations.").

that adds little or nothing to the accuracy of the Commission's determination.

Respectfully submitted,

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ATTACHMENT A

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RPGI MEMBERS

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City of Afton
City of Buffalo
City of Danville
City of Guttenberg (as of 01/01/2019)
City of Pocahontas
City of West Liberty
Coggon Municipal Utilities
Dysart Municipal Utilities
Farmers Electric Cooperative–Kalona
Grand Junction Municipal Utilities
Hopkinton Municipal Utilities
La Porte City Utilities
Long Grove Municipal Electric Utilities
Mt. Pleasant Municipal Utilities
New London Municipal Utilities
Odgen Municipal Utilities
Sibley Municipal Utilities
State Center Municipal Utilities
Story City Municipal Electric Utility
Tipton Municipal Utilities
Traer Municipal Utilities
Vinton Municipal Electric Utility
West Point Utility System
Whittemore Municipal Utilities