BEFORE THE FEDERAL ENERGY REGULATORY COMMISSION

PJM Interconnection, L.L.C.,	**)**	**Docket ER17-211-000**
Mid-Atlantic Interstate Transmission, LLC.	**)**	

PROTEST AND REQUEST FOR HEARING OF THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

James P. Melia
Aspassia V. Staevska
Counsel for the Pennsylvania Public Utility Commission
PO Box 3265
Harrisburg, PA 17105-3265
Tel: 717-787-1859
jmelia@pa.gov
astaevska@pa.gov

Pursuant to Rule 211 of the Federal Energy Regulatory Commission's Rules of Practice and Procedure, 18 C.F.R. §385.211, the Pennsylvania Public Utility Commission (PAPUC) herein files its Protest and Request for Hearing in response to the filing of Mid-Atlantic Interstate Transmission (MAIT) at this docket seeking establishment of a formula rate.

I. INTRODUCTION

On October 28, 2016, MAIT, a newly-formed affiliate of First Energy (FE) filed a request for approval of a change in the revenue requirement used to establish the transmission rates charged for the Metropolitan Edison Company (Met- Ed) and Pennsylvania Electric Company (Penelec) Zones under the PJM Interconnection, L.L.C. (PJM) Open Access Transmission Tariff (OATT).[1] The change in rates will be accomplished by adding a transmission formula rate template and formula rate protocols set forth in PJM's OATT. MAIT is a newly-formed, stand-alone transmission company that has received regulatory approval to acquire the FERC-jurisdictional electric transmission facilities owned by MetEd and Penelec. MAIT expects the transaction to close on December 31, 2016. The impact of the proposed revenue rate increase for Pennsylvania customers will be a 47% increase in transmission rates and an annual revenue requirement of $131 million.

[1] *PJM Interconnection L.L.C., Mid-Atlantic Interstate Transmission L.L.C.*, Docket No. ER17-211.

The PAPUC has reviewed and analyzed the filing and contends that the requested Return on Equity (ROE) is not just and reasonable given current market conditions and that MAIT's formula rate template and protocols are not just and reasonable nor are they consistent with FERC precedent regarding forward-looking transmission formula rates.

II. PROTEST

The PAPUC raises the following issues as a basis for its protest:

A. MAIT's Proposed Return On Equity Has Not Been Shown To Be Just And Reasonable

MAIT witness Adrien McKenzie presents testimony and exhibits supporting a return on equity of 10.5% with a 50-basis point adder for a requested ROE of 11.0%.[2] Mr. McKenzie primarily relies on the FERC-approved two-step Discounted Cash Flow (DCF) Model set forth in FERC Orders Nos. 531 and 551.[3] Mr. McKenzie then supplements his DCF analysis with application of the risk premium method, Capital Asset Pricing Method (CAPM) and the expected earnings approach. Finally, Mr. McKenzie measures these individual ROE determinations against several benchmarks including gas pipeline ROEs, projected bond yields, examination of a low-risk non-utility DCF model and examination of

[2] MAIT Attachment 5 (Prepared Direct Testimony and Exhibits of Adrien M. McKenzie).

[3] *Coakley v. Bangor Hydro Elec. Co.*, Opinion No. 531, 147 FERC ¶ 61,234, *order on paper hearing*, Opinion No. 531-A, 149 FERC ¶ 61,032 (2014), *order on reh'g*, Opinion No. 531-B, 150 FERC ¶ 61,165 (2015), *appeals docketed sub nom. Emera Maine v. FERC*, Nos. 15-1118, *et al.* (D.C. Cir. Apr. 30, 2015); *Ass'n of Businesses Advocating Tariff Equity v. Midcontinent Indep. Sys. Operator, Inc.*, Opinion No. 551, 156 FERC ¶ 61,234 (2016), *reh'g pending*.

a Value Line-Based DCF Study. While Mr. McKenzie's methodologies are fairly well-accepted, there are incorrect assumptions and reliance on biased data that unrealistically inflate the ROE recommendation.

1. MAIT Fails To Demonstrate That Anomalous Market Conditions Exist

Mr. McKenzie places heavy emphasis on language in FERC Orders 531 and 551 characterizing current market conditions involving "atypically" low interest rates and unreasonably low 10-year and 30-year Treasury bond rates as anomalous and unlikely to continue into the future.[4] Mr. McKenzie also argues that long term bond yields have been artificially suppressed due to the "Federal Reserve's unprecedented intervention in the capital markets."[5] Mr. McKenzie concludes that the collateral consequences of anomalous capital market conditions impacts the screen used for eliminating low-end DCF results. Further, Mr. McKenzie states that the DCF outcomes produced by using the Commission's method of eliminating low-end DCF results by adding 100 basis points to historical bond yields produces a result that is too low and does not reflect investors' required returns going forward.[6] The impact of not using the Commission's method for screening low-end DCF estimates has the effect of eliminating DCF results that would have otherwise been considered in the range of reasonableness, ultimately

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[4] Direct Testimony of Adrien M. McKenzie at 39-45.
[5] *Id.* at 44.
[6] *Id.* at 47.

producing higher DCF results. Mr. McKenzie also argues for consideration of various other alternative benchmarks all of which result in higher ROEs than the FERC- approved DCF model.[7]

The PAPUC is not convinced that Mr. McKenzie's adjustments, based on anomalous economic conditions allowed by FERC in Orders 531 and 551, are still justified given the long term stability of factors such as interest rates, Treasury bond yields and corporate bond yields (both utility and non-utility) in the near term.

It is also worth noting that FERC rejected the use of Value Line generally as a source for short-term growth rates in Opinion 551instead expressing a preference for Institutional Broker's Estimate System (IBES) growth rates.[8]

Mr. McKenzie contends interest rates are atypically low. However these low interest rates have been entrenched since 2008. Eight years later there has been little upward movement in rates. This trend suggests the Federal Reserve monetary policy is no longer anomalous; rather this is a new normal of lower interest rates. John C. Williams, President and CEO, Federal Reserve Bank of San Francisco stated the following:

> "This policy path should be viewed in the context of an economy that has mostly cleared the Great Recession but faces

[7] *Id.* at 48.
[8] Opinion 551 at ¶¶62-64.

a future that looks very different from the past in important ways. Although the natural rate of unemployment appears close to what it was a decade ago, demographic trends and a sustained productivity slowdown have pushed down the normal growth rates of jobs and GDP and have lowered the normal rates of interest. These developments will shape the economic landscape for years to come."[9]

The PAPUC also notes in its supporting affidavit of David Huff, Analyst for the PAPUC Staff, that recent U.S. published statistics on interest rates for corporate bonds, municipal bonds, federal funds, Treasury bills and Treasury securities have been remarkably stable, all pointing to the current conditions being the new normal.[10] For example, industry analysts are projecting the following for several important economic indices:

Federal Funds Rate	**10 Year U.S. Treasuries**	**Consumer Price Index**
1st Quarter 2017: 0.7%	1st Quarter 2017: 1.9%	1st Quarter 2017: 2.2%
1st Quarter 2018: 1.2%	1st Quarter 2018: 2.5%	1st Quarter 2018: 2.3%[11]

The PAPUC files this protest to MAIT witness McKenzie's unjustified reliance on the persistence of so-called "anomalous conditions" as one rationale for deriving higher than justified ROEs through elimination of certain DCF results and reliance on other benchmarks. The PAPUC contends this issue should be assigned for evidentiary hearing.

[9] Presentation to the Federal Home Loan Bank of San Francisco's 2016 Member Conference, San Francisco, CA by John C. Williams, President and CEO, Federal Reserve Bank of San Francisco, October 21, 2016.
[10] *See* Affidavit of David A. Huff and Exhibit attached to this Protest.
[11] Interest rates and CPI from *Blue Chip Financial Forecasts*, *Vol. 35, No. 11, November 1, 2016.*

2. MAIT Improperly Includes Avangrid In Its Proxy Group

Mr. McKenzie includes Avangrid as a part of its electric utility proxy group for purposes of his DCF analysis.[12] Avangrid is an electric and gas utility operating throughout New York and New England. Avangrid is the result of a merger between UIL Holdings Corporation and Iberdrola in 2015. Mr. McKenzie states that Avangrid is not included in the Value Line electric utility group due to its recent creation although all other members of the electric utility proxy group are included in Value Line.[13]

The PAPUC submits that inclusion of Avangrid was solely for purposes of inflating the ROE range of reasonableness and ultimately MAIT's recommended ROE. The affidavit of Mr. Huff presents the PAPUC's position. For example, McKenzie uses *Yahoo! Finance* which utilizes IBES short-term growth rates used in the two-step DCF calculation. McKenzie cites to a short-term growth rate of 9.00%, however Avangrid is currently showing a short-term growth rate of 8.00%.[14] Using the *Yahoo! Finance* provided 8.00% growth rate results in Avangrid having a 6.78% weighted growth rate and an 11.09% cost of equity.[15]

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[12] The discounted cash flow analysis has two components: dividend yield and growth rate. *See* McKenzie Exhibit No. MAT-11 at 2.
[13] McKenzie Testimony at 22-23.
[14] McKenzie Exhibit No. MAT-12 at 1.
[15] *Yahoo! Finance* Growth Rate dated November 1, 2016.

The PAPUC notes that eliminating Avangrid from the DCF IBES Growth Model, (Exhibit No. MAT-12, p.1), significantly reduces the top end of the ROE range of reasonableness. For example, the top end of the DCF range drops from 11.76% to 9.75%, the top-end midpoint would drop to 9.32% and the top-end median would remain at 8.42%. Simply eliminating Avangrid from McKenzie's proxy group would drop the top-end of the range ROE to below 10%.

Avangrid's business profile includes the ownership and operation of a significant portion of natural gas distribution and renewable generation assets. Calculating the ROE of a firm by using another firm as a proxy requires one to choose a proxy operating in markets with equivalent risk, thereby resulting in the expectation of a comparable rate of return. No proxy company has the exact same risk or growth profile. However, Avangrid's operations in both natural gas distribution and renewable generation make the firm a less-than-ideal equivalent risk proxy that unreasonably inflates the growth component in MAIT's ROE calculations.

Additionally, the PAPUC contends that Avangrid should not be used in the proxy group because it does not meet the proxy group criteria set by McKenzie himself, specifically inclusion in Value Line. Avangrid has been in existence for less than a year and its performance as an electric utility is not well established. Avangrid also has a large investment in wind power assets and is heavily invested in the natural gas utility business rather than the electric utility business making it a less than ideal candidate as an electric utility. Based on the foregoing characteristics, Avangrid should be removed from any proxy group consideration. The PAPUC requests that this issue as well as the propriety of MAIT's proxy group selection generally be assigned to an evidentiary hearing.

3. The DCF Value Line Growth Rate Model Is Artificially Inflated By PG&E

Mr. McKenzie's DCF Value Line growth rate model at Exhibit No. MAT-19 is inflated by the inclusion of a Value Line growth component for Pacific Gas & Electric (PG&E) of 12.0% that is far in excess of other growth rates in the electric utility proxy group. While Value Line does calculate an annual growth rate estimate of 12% for the 2013-2015 to the 2019-2021 timeframe, PG&E had a negative 5.5% growth rate for the past 5 years and 0.5% for the past ten years.[16] Since a gas pipeline explosion in September 2010, the company has been incurring costs associated with the accident, including unrecovered capital costs associated with upgrading its gas system. This is why earnings have generally been weak since 2010.[17] If we calculate an EPS annual growth rate from 2009 to 2019, we see a more modest annual growth rate of 4.03%.[18]

[16] *Value Line Summary* October 29, 2016, prepared by Paul E. Debbas, CFA
[17] *Id.*
[18] Value Line lists a 2009 EPS of $3.03 and an estimated 2019-2021 EPS of $4.50.

On this basis, the PAPUC contends the PG&E 12% annual earnings growth rate is inaccurate, misleading and skews the results. This growth rate fails to account for the effects of an outsized event that clearly depressed the company's earnings per share number for several years. Excluding PG&E would reduce the top-end of the range of reasonableness from 12.76% to 10.81%, nearly a 200 basis point difference.

The PAPUC contends that MAIT's selection of PG&E for inclusion in its electric utility proxy group may result in an unjust and unreasonable ROE amount. The PAPUC requests this issue to be assigned for an evidentiary hearing.

4. MAIT's Projected Implied Bond Yield Is Excessive

Mr. McKenzie suggests that using a 100 basis point spread above the 6-month historical average equivalent public utility bond yield to remove low-end ROE outliers, as referenced in FERC Orders 531 and 551, does not accurately remove low-end values.[19] He further states that adding a margin of 100 basis points is insufficient to reflect investors' required returns going forward. Mr. McKenzie advocates instead for a projected implied bond yield based on data derived from IHS Global Insight and the Energy Information Administration non-equivalent Aa rated debt for the 2017-2021 timeline. McKenzie supports this

[19] McKenzie Testimony at 30.

conclusion by citing to economic studies showing that risk premiums are higher when interest rates are at very low levels.[20]

Mr. McKenzie calculates an average 2017-2021 AA utility bond rate of 5.46% based on EIA 2016 data of 5.50% and IHS Global Insight of 5.41%. Mr. McKenzie then adds a 0.94% current BAA-Aa Yield Spread to arrive at an Implied Baa Utility Yield of 6.4%.[21]

The PAPUC has examined Mr. McKenzie's analysis and believes his projections of bond yields are unrealistically inflated. The PAPUC contends there is no market data to support the assumption that bond yields have so drastically changed since the issuance of FERC Orders 531 and 551 to justify departing from FERC's guideline of the 100 basis point margin above the historical public utility bond yield. McKenzie has calculated the historical bond yield to be 4.55%.[22] Adding the 100 basis point margin to the historic bond yield results in an interest rate of 5.55% that is well below the 6.40% advocated by Mr. McKenzie.

The PAPUC contends that Mr. McKenzie's projected interest rates may be unreasonably high because other industry sources identify lower current bond yield projections. For example, Blue Chip Financial Forecasts Long-Range Survey for a

[20] *Id.* at 30-31.
[21] *Id.* at 31
[22] MAIT Exhibit No. MAT-17 at 1.

Corporate Aaa bond yield has experienced a noticeable downshift in the projections as follows:

Blue Chip Survey of Corporate Aaa Bond Yield (6/1/2015):

2017	5.4%
2018	5.8%
2019	5.9%
2020	6.1%
2021	6.1%
2017-2021	5.9%

Blue Chip Survey of Corporate Aaa Bond Yield (6/1/2016):

2018	5.1%
2019	5.4%
2020	5.5%
2021	5.5%
2022	5.5%
2018-2022	5.4%[23]

Mr. McKenzie's recommendation to abandon FERC's 100 basis point adder standard should be rejected. Further, given that bond yields have not risen as projected by financial forecasters, Mr. McKenzie's Implied Baa Utility yield is overstated and should not be relied upon as a guide to evaluate the low end range of his DCF range. The PAPUC protests MAIT's filing on this basis and requests this issue be assigned for evidentiary hearing.

[23] *Blue Chip Financial Forecasts Long-Range Survey for a Corporate Aaa Bond* Volume 34, No.6 (6/1/2015) and Volume 35, No.6 (6/1/2016).

5. MAIT's Proposal To Include A 50 Basis Point Adder For RTO Membership Is Unjust And Unreasonable

MAIT requests an incentive adder of 50 basis points to its requested ROE of 10.5% to award MAIT for its membership in PJM. Mr. McKenzie's testimony reiterates that FERC's standard policy has always been to reward transmission companies an RTO participation adder.[24]

The PAPUC protests MAIT's request for an additional 50 basis point "incentive" over and above MAIT's requested 10.5% ROE. MAIT is requesting an incentive for which it has done nothing other than to transfer facilities. The transmission facilities which constitute MAIT were transferred from FE affiliates Penelec and MetEd that have been longstanding members of PJM. In fact, MAIT had little choice but to continue to participate in PJM considering MetEd's and Penelec's existing contractual commitments to PJM under the OATT. In short, MAIT is already effectively tied to PJM which makes the concept of "choosing to join an RTO" largely illusory. The PAPUC protests the MAIT filing on the basis that its request for a 50 basis point incentive is unjust and unreasonable.

The PAPUC requests that this issue be set for evidentiary hearing.

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[24] McKenzie Testimony at 16.

B. MAIT's Proposed Formula Rate Protocols Have Not Been Shown To Be Just And Reasonable

MAIT witness Roger Ruch proposes a Formula Rate Template and Protocol that is based on the recently-approved MISO Protocols.[25] In the PAPUC's view, it is more appropriate to compare MAIT's protocols to existing ATSI protocols for several reasons: (1) ATSI and MAIT are both subsidiaries of the same company, FirstEnergy Transmission (FET) and share the same corporate parent and corporate plan for transmission growth, Energizing the Future (EtF); (2) both ATSI and MAIT operate in the same RTO—PJM—which is distinct and different from MISO and operates under a different transmission tariff and related agreements; (3) the ATSI Tariff and Protocol were subject to settlement discussions that arrived at a just and reasonable result for ATSI and its customers and were subsequently approved by FERC[26]; and (4) MAIT customers bear a closer relationship to ATSI customers than MISO customers, by virtue of their participation and physical location in PJM. Therefore, it is more appropriate to design the MAIT Protocol to conform to the ATSI model as opposed to the MISO model.

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[25] Testimony of Roger D. Ruch at 5-19 (MAIT Exhibit No. MAT-1).

[26] *American Transmissions Systems, Inc.*, 153 FERC ¶ 61,106 (2015). *See also* OATT Attachment H-21A, OATT Attachment H-21A - ATSI, 3.2.0, OATT Attachment H-21A Appendix D, OATT Attachment H-21A Appendix D - ATSI, 1.1.0, OATT Attachment H-21A App D, OATT Attachment H-21A Appendix D (True-up), 0.2.0 , OATT Attachment H-21A Appendix E, OATT Attachment H-21A Appendix E - ATSI, 1.1.0, OATT Attachment H-21A App E, OATT Attachment H-21A Appendix E (True-up), 0.2.0, OATT Attachment H-21A Appendix H, OATT Attachment H-21A Appendix H, 0.2.0, OATT Attachment H-21B, OATT Attachment H-21B - ATSI Protocol, 1.2.0.

Upon a close review, MAIT's Protocol is very similar to ATSI's Protocol, with several notable omissions related to cost transparency and information sharing with interested parties. ATSI's Protocol specifically allows interested parties to request information from the transmission owner about how transmission projects and purchases of capital equipment are identified, forecasted, evaluated and selected for inclusion in the following Rate Year or Projected Transmission Revenue Requirement (PTRR).[27] MAIT's proposed Protocol is silent on these important factors. Additionally, MAIT's proposed Annual Projected Rate Meeting described in Section II (H) of MAIT's Protocol significantly shortens the notice period to be provided by MAIT to interested parties, as compared to the same provision in the ATSI Protocol,[28] thus giving interested parties unreasonably short time to review information provided by MAIT and seek clarification. Furthermore, MAIT's Information Exchange Provisions in Section III of the Protocol omit the provisions in the ATSI Protocol that allow parties to seek information about the reasonableness of costs and expenditures in the Actual Transmission Revenue Requirement (ATRR) and PTRR, procurement methods, cost control methodologies, cost allocation determinations and need.[29] Similarly, the Formal Challenge procedures in the MAIT Protocol exclude challenges available in the

[27] ATSI Protocol, Section II (C) and (D).
[28] ATSI Protocol, Section II (I)
[29] ATSI Protocol, Section III (A) 5 and 6.

ATSI Protocol related to the reasonableness and need of costs and expenditures in the ATRR and PTRR.[30]

Moreover, MAIT's new provision[31] allowing it to unilaterally modify, through a Section 205 filing, stated values in the Formula Rate for (a) amortization and depreciation rates, (b) post-employment benefits other than pension rates or (c) the weighting of the ADIT balance in the rate base to ensure MAIT's compliance with the IRS regulations for normalization under IRS Section 1.167(l)-1(h)(6), is not just and reasonable. MAIT has not demonstrated why these matters cannot be addressed in the current Formula Rate filing and has not substantiated the need to make, at its discretion and at a time of its choosing, single issue Section 205 Filings.

Also, notably missing from the MAIT Protocol is the provision in the ATSI Protocol that obligates the transmission owner to make good faith corrections of errors identified in its Annual Update or FERC Form No. 1.[32]

Given MAIT's ambitious plans to implement its EtF program, which relies, to a large extent, on reliability enhancement projects that are identified, selected, and implemented not by PJM, but by FE, it is imperative to provide as much

[30] ATSI Protocol, Section IV (C) 1 c. (v), (vi), and (vii); (D) 6 and 7.
[31] MAIT Protocol, Section IV (I).
[32] ATSI Protocol, Section V (B).

transparency as possible, subject to confidentiality provisions, to MAIT's customers and other interested parties, such as the PAPUC. The Commission has already noted in its Order to Show Cause at Docket No. EL16-71 that supplemental projects, like MAIT's reliability enhancement projects, and the transmission owner's criteria for their selection, need to be transparent to customers.[33] MAIT's proposed Protocols are a step back from that direction and require, at a minimum, the addition of the ATSI provisions described herein.

For these reasons, the PAPUC files its Protest on this issue and requests that the matter be set for an evidentiary hearing.

C. MAIT's Proposal To Recover "Extraordinary Vegetation Management Costs" Has Not Been Shown To Be Just And Reasonable

MAIT requests recovery of approximately $16.9 million of previously expended vegetation management costs associated with MetEd and Penelec activities. MAIT proposes to recover these expenses over a seven–year period beginning with the effective date of the formula rate.[34]

The PAPUC protests MAIT's proposed recovery of these costs. The expenses for which recovery is being sought should have been recovered

[33] *Order to Show Cause re: Monongahela Power et al* at Docket No. EL16-71 (issued August 26, 2016).
[34] Direct Testimony of Marlene R. Barwood at 9-10.

previously through rates for Penelec and MetEd. There is no indication that these costs have not already been recovered. Seeking recovery through formula rates would constitute potentially retroactive ratemaking or double recovery. The PAPUC requests that this issue be assigned to an evidentiary hearing.

D. MAIT's Proposal To Recover "Startup Costs" Has Not Been Shown To Be Just and Reasonable

MAIT requests recovery of "startup costs" – fees and costs associated with seeking regulatory approvals that will permit MAIT to begin commercial operations. These costs amount to about $1.1 million and would be recovered by way of amortization over a 12-month period.[35]

The PAPUC protests MAIT's proposed recovery of these costs. In a recent PAPUC approved settlement of FE's proposed transfer of transmission facilities to MAIT, FE committed to not seeking recovery of any start-up costs associated with the formation of MAIT.[36] In the PAPUC Order approving the settlement, the parties agreed as follows:

> 27. Joint Applicants commit to exclude all costs to achieve the Transaction (i.e., both Transaction-related and transition costs associated with the transfer of assets) from distribution and transmission rates. For purposes of

[35] Direct Testimony of Marlene R. Barwood at 10-11.
[36] *Joint Application of Mid-Atl. Interstate Transmission, LLC ("MAIT"); Metro. Edison Co. ("Met-Ed") and Pa. Elec. Co. ("Penelec"),* Docket Nos. A-2015-2488903, *et al.*, Opinion and Order at 9-10. (Order issued July 21, 2016).

> this paragraph, "transition costs" are defined as costs to integrate assets into the acquiring utility as a result of the Transaction, and are incurred after the Transaction is consummated. Transition costs include components such as, internal costs of employees spending time working on transition issues; external costs paid to consultants and advisers; operational integration costs; accounting and operating systems integration costs; and costs to terminate any duplicative leases, contracts, and operations. Additionally, for purposes of this paragraph, "transfer of assets" refers to the transfer of assets that will occur upon obtaining all necessary approvals requested in the following: (i) the Joint Application file in this proceeding; (ii) the NJBPU Proceeding and (iii) the FERC Proceeding (approval obtained on February 18, 2016). Joint Applicants expect that the transition period for the Transaction will be no more than one year.

MAIT's claim in this proceeding raises questions regarding its commitment to adhere to the terms of its settlement before the PAPUC. The PAPUC requests that this issue be assigned to an evidentiary hearing.

E. MAIT's Filing Is Deficient In Detailing The Reliability Enhancement Costs Which Are The Subject Of The Filing

MAIT notes at p. 7 of its cover letter that the purposes of its request for formula rates is to implement its EtF program to increase the reliability of the FE transmission system with reference to both Transmission Planning Projects and Reliability Enhancement Projects. The description of the Etf program in its cover letter is generalized in nature with no specifics. MAIT's testimony and exhibits are silent on the types of projects and the associated costs that will be supported by its proposed formula rate. The PAPUC is particularly interested in examining the details of MAIT Reliability Enhancement Projects which are allegedly focused on enhancing customer service, upgrading the health of the existing system, enhancing system performance, increasing operational flexibility and grid security. Many of these projects may be considered to be supplemental transmission projects which are projects not subject to the normal scrutiny accorded certain projects under the PJM Regional Transmission Expansion Plan (RTEP) process. FERC has recently initiated a proceeding at Docket No. EL16-71 to examine issues surrounding supplemental transmission projects.[37] The PAPUC and the parties should have the opportunity to examine the specific projects that underlay MAIT's request for formula rates.

For these reasons, the PAPUC requests that the issues raised by MAIT's claim for recovery of Reliability Enhancement costs be assigned for an evidentiary hearing.

F. The PAPUC Requests An Evidentiary Hearing And Further Requests The Maximum 5-Month Suspension Of The Effective Date Of The Proposed Formula Rates

MAIT's filing proposes a revenue increase of 46% over current rates and will amount to an annual revenue requirement of $131 million. The impact on

[37] *Order to Show Cause re: Monongahela Power et al* at Docket No. EL16-71 (issued August 26, 2016).

Pennsylvania ratepayers will be significant and permanent. MAIT's filing raises serious issues of material fact with regard to its ROE proposal, the formula rate protocols and underlying reliability enhancement projects that are the basis of the filing. These issues deserve careful examination. For example, MAIT's stated but largely unsubstantiated intent to implement investments under its EtF Program is laudable but the filing is lacking in the details of those investments. The PAPUC has a statutory obligation to protect its ratepayers from exorbitant and possibly imprudent transmission investment. Moreover, other parties to this proceeding should have ample time to fully investigate the details of this filing. Consequently, the PAPUC requests that this matter be assigned for an evidentiary hearing and be suspended for the full five month period pursuant to 16 U.S.C. § 824d(e) and that a refund effective date be established.

G. The PAPUC Reserves The Right To Supplement Its Protest

The PAPUC reserves the right to identify additional issues based on discovery by it and other parties to the case and to supplement its Protest.

III. CONCLUSION

WHEREFORE, the Pennsylvania Office of Consumer Advocate respectfully requests that the Commission: (1) deny Applicants' request to accept without a hearing or suspension the proposed formula rate template and protocols, (2) suspend the effective date for a period of five months, (3) establish a refund effective date; and (4) schedule this matter for an evidentiary hearing.

Respectfully submitted,

/s/ James P. Melia
James P. Melia
Aspassia V. Staevska
Counsel for the Pennsylvania Public
Utility Commission
PO Box 3265
Harrisburg, PA 17105-3265
Tel: 717-787-1859
jmelia@pa.gov

Dated: November 30, 2016

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I am on this date serving a copy of the foregoing document upon each person designated on the official service list compiled by the Federal Energy Regulatory Commission in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure.

Dated at Harrisburg, PA this 30th day of November, 2016.

Respectfully submitted,

/s/ James P. Melia
James P. Melia

Counsel for the Pennsylvania
Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265
Tel: (717) 787-5000

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Promoting Transmission Investment Through Pricing Reform	**)** **)**	**Docket ER17-211-000**

Affidavit of David L. Huff

I, David Huff, being duly sworn, depose and say:

1. My name is David L. Huff. I am currently employed by the Pennsylvania Public Utility Commission (PAPUC) as the Supervisor of the Finance section in the PAPUC's Bureau of Technical Utility Services. I have a Masters of Business Administration Degree with a concentration in finance and over 30 years of experience working for a regulated public utility and/or for a public utility regulatory agency. This experience includes thirteen years of experience analyzing financial filings and utility rate filings for the PAPUC and 17 years of work experience working for GTE Telephone Operations, and following its merger with Bell Atlantic, Verizon. While at both GTE and Verizon, I had a broad range of responsibilities in areas such as accounting operations, regulatory accounting, business sales, strategic planning and budgeting, pricing and wholesale account management. While working for GTE and Verizon, I was involved in the preparation of financial schedules for rate case proceedings,

earnings monitoring reports and price cap filings for the Federal Communications Commission. At the PAPUC, I supervise a staff that provides technical assistance to the Commission and the Commission's Office of Administrative Law Judges in determining a utility's rate of return in rate proceedings, provide rate of return schedules and analysis in small water and gas utility filings, provide return on equity analysis for the PA PUC's quarterly earnings monitoring report, write draft Orders for securities registration, mergers and change of control applications, and affiliated interest agreement application, and write detailed reports on financial matters as they relate to regulatory policy. My qualifications are attached as an appendix to this application.

2. The purpose of this affidavit is to provide comments in support of the Protest of the PAPUC to the recent filing of Mid-Atlantic Interstate Transmission (MAIT) for the establishment of a formula rate. MAIT is a newly-formed, stand-alone transmission company that has received regulatory approval to acquire the FERC-jurisdictional electric transmission facilities owned by Met-Ed and Penelec. MAIT expects the transaction to close on December 31, 2016. The impact of the proposed revenue rate increase for Pennsylvania customers will be a 47% increase in transmission rates and an annual revenue requirement of $131 million.

3. I have reviewed and analyzed the Testimony and Exhibits of MAIT witness Adrien M. McKenzie. Mr. McKenzie recommends a return on equity

(ROE) of 10.5 % coupled with a 50 basis point incentive adder for RTO membership resulting in an overall ROE of 11.0%. Mr. McKenzie primarily relies on the FERC-approved two-step Discounted Cash Flow (DCF) Model set forth in FERC Orders Nos. 531 and 551. Mr. McKenzie then supplements his DCF analysis with application of the risk premium method, Capital Asset Pricing Method (CAPM) and the expected earnings approach. Finally, Mr. McKenzie measures these individual ROE determinations against several benchmarks including gas pipeline ROEs, projected bond yields, examination of a low-risk non-utility DCF model and examination of a Value Line-Based DCF Study.

4. My review and analysis of Mr. McKenzie's ROE recommendation concludes that his overall analyses, while traditionally sound, utilizes incorrect assumptions and relies on biased data to inflate his ROE recommendation.

5. Mr. McKenzie relies on language in FERC Orders 531 and 551 characterizing current market conditions involving atypically low interest rates and unreasonably low 10-year and 30-year Treasury bond rates as anomalous and unlikely to continue into the future. Mr. McKenzie also argues that long term bond yields have been artificially suppressed due to the "Federal Reserve's unprecedented intervention in the capital markets." Mr. McKenzie concludes that "the collateral consequences of anomalous capital market conditions impacts the screen used for eliminating low-end DCF results." Mr. McKenzie further states

that the DCF outcomes produced by using the Commission's method of eliminating low-end DCF results by adding a 100 basis points to historical bond yields produces a result that is too low and does not reflect investor's required returns going forward. The impact of not using the Commission's method for screening low-end DCF estimates has the effect of eliminating DCF results that would have otherwise been considered in the range of reasonableness, ultimately producing higher DCF results. Mr. McKenzie also argues for consideration of various other alternative benchmarks all of which result in higher ROEs than the FERC approved DCF model.

6. My review of current financial market data and other economic sources convinces me that Mr. McKenzie's assumption that existing stable market conditions since the recovery from the recession of 2008 are not anomalous but constitute a new normal. For example, recent U.S. published statistics on interest rates for corporate bonds, municipal bonds, federal funds, Treasury bills and Treasury securities have been remarkably stable, all pointing to the current conditions as being the new normal. For example, industry analysts are projecting the following for several important economic indices:

Federal Funds Rate	**10 Year U.S. Treasuries**	**Consumer Price Index**
1st Quarter 2017: 0.7%	1st Quarter 2017: 1.9%	1st Quarter 2017: 2.2%
1st Quarter 2018: 1.2%	1st Quarter 2018: 2.5%	1st Quarter 2018: 2.3%[1]

[1] Interest rates and CPI from _Blue Chip Financial Forecasts_, *Vol. 35, No. 11, November 1, 2016.*

Mr. McKenzie's proposal to not use the Commission's methodology to screen for the elimination of low-end DCF results is only done for the purpose of producing higher DCF results. On this basis, Mr. McKenzie's DCF analysis raises sufficient doubts regarding the justification for his proposed ROE analysis to warrant evidentiary hearings on this matter.

7. Mr. McKenzie includes Avangrid as a part of his electric utility proxy group for purposes of his DCF analysis. Avangrid is an electric and gas utility operating throughout New York and New England. Avangrid is the result of a merger between UIL Holdings Corporation and Iberdrola in 2015. Mr. McKenzie states that Avangrid is not included in the Value Line electric utility group due to its recent creation, although all other members of the electric utility proxy group are included in Value Line.

8. The PAPUC notes that eliminating Avangrid from the DCF IBES Growth Model, (Exhibit No. MAT-12, p.1) reduces the top end of the ROE range of reasonableness. For example, the top end of the DCF range drops from 11.76% to 9.75%, the top-end midpoint would drop to 9.32% and the top-end median would remain at 8.42%. Simply eliminating Avangrid from McKenzie's proxy group would drop the top-end of the range ROE to below 10.0%. Further, I do not believe that Avangrid should be used in the proxy group because it does not meet the proxy group criteria set by Mr. McKenzie himself, specifically inclusion in

Value Line. Avangrid has been in existence for less than a year and its performance as a newly merged electric utility is not well established. Avangrid also has a large investment in wind power assets and is heavily invested in the natural gas utility business rather than the electric utility business making it a less than ideal candidate as an electric utility. Based on the foregoing characteristics, I believe that Avangrid should be removed from any proxy group consideration.

9. I have also reviewed Mr. McKenzie's Value Line growth rate model. Mr. McKenzie's DCF Value Line growth rate model at Exhibit No. MAT-19 is inflated by inclusion of a Value Line growth component for Pacific Gas & Electric (PG&E) of 12.0% that is far in excess of other growth rates in the electric utility proxy group. While Value Line does calculate an annual growth rate estimate of 12.0% for the 2013-2015 to the 2019-2021 timeframe, PG&E had a negative 5.5% growth rate for the past 5 years and 0.5% for the past ten years.[2] Since a gas pipeline explosion in September 2010, the company has been incurring costs associated with upgrading its gas system which is why earnings have generally been weak.[3] If we calculate an EPS annual growth rate from 2009 to 2019, we see a modest annual growth rate of 4.03%.[4]

[2] *Value Line Summary* October 29, 2016, prepared by Paul E. Debbas, CFA.
[3] *Id.*
[4] Value Line lists a 2009 EPS of $3.03 and an estimated 2019-2021 EPS of $4.50.

10. On this basis, I believe that PG&E 12.0% annual earnings growth rate is misleading and skews the results of the entire growth rate model. This growth rate fails to account for the effects of an extraordinary event that depressed the company's earnings per share number for several years. Excluding PG&E would reduce the top-end of the range of reasonableness from 12.76% to 10.81% -- nearly a 200 basis point difference. I believe that PG&E should be eliminated from Mr. McKenzie's growth rate model.

11. I also disagree with Mr. McKenzie's projected implied bond yield. Mr. McKenzie suggests that using a 100 basis point spread above the 6-month historical average public utility bond yield to remove low-end ROE outliers, as referenced in FERC Orders 531 and 551, does not accurately remove low-end values. He further states that adding a margin of 100 basis points is too low to reflect investors' required returns going forward. Mr. McKenzie advocates instead for a projected implied bond yield based on data derived from IHS Global Insight and the Energy Information Administration for the 2017-2021 timeline. Mr. McKenzie supports this conclusion by quoting economic studies showing that risk premiums are higher when interest rates are at very low levels, but fails to cite a specific study.

12. Mr. McKenzie calculates an average 2017-2021 AA utility bond rate of 5.46% based on EIA 2016 data of 5.50% and IHS Global Insight data of 5.41%.

Mr. McKenzie then adds a 0.94% current BAA-Aa Yield Spread to arrive at an Implied Baa Utility Yield of 6.4%.

12. I have examined Mr. McKenzie's analysis and I believe his projections of bond yields are unrealistically inflated. I have not reviewed any market data to support the assumption that bond yields have so drastically changed since the issuance of FERC Orders 531 and 551 to justify departing from FERC's guideline of the 100 basis point margin above the historical public utility bond yield. McKenzie has calculated the historical bond yield to be 4.55%. Adding the 100 basis point margin to the historic bond yield results in an interest rate of 5.55% that is well below the 6.40% advocated by Mr. McKenzie.

13. Mr. McKenzie's projected interest rates may be unreasonably high because other industry sources identify lower current bond yield projections. For example, Blue Chip Financial Forecasts Long-Range Survey for a Corporate Aaa bond yield has experienced a noticeable downshift in the projections as follows:

Blue Chip Survey of Corporate Aaa Bond Yield (6/1/2015):

2017	5.4%
2018	5.8%
2019	5.9%
2020	6.1%
2021	6.1%
2017-2021	5.9%

Blue Chip Survey of Corporate Aaa Bond Yield (6/1/2016):

2018	5.1%
2019	5.4%
2020	5.5%
2021	5.5%
2022	5.5%
2018-2022	5.4%[5]

15. I conclude that Mr. McKenzie's recommendation to abandon FERC's 100 basis point adder standard should be rejected. Further, given that bond yields have not risen as projected by financial forecasters, Mr. McKenzie's Implied Baa Utility yield is overstated and should not be relied upon as a guide to evaluate the low end range of his DCF range.

16. This concludes my affidavit.

[5] *Blue Chip Financial Forecasts Long-Range Survey for a Corporate Aaa Bond* Volume 34, No.6 (6/1/2015) and Volume 35, No.6 (6/1/2016).

Appendix

Educational and Professional Background Of David L. Huff

<u>Professional Experience</u>

Current Work Experience/Training:

July 2012 to Present: Bureau of Technical Utility Services, Finance Division, Pennsylvania Public Utility Commission, Harrisburg, Pennsylvania.

Supervisor Finance Section:

- Supervises a staff of six Financial Analysts in the preparation of complex technical reports and recommendations in response to utility filings, utility initiatives, Commissioner inquiries and request from other bureaus within the PAPUC.
- Supervise analyst in their review of securities filings, change of control applications, affiliated interest filings, tariff changes and tax matters filed by natural gas distribution, electric distribution, water and wastewater distribution, pipeline operators, telephone and other fixed utilities operating in the Commonwealth.
- Reviews draft Commission Orders and Reports for securities registration, mergers and change of control applications, tariff compliance and affiliated interest agreements.
- Provide both written and oral testimony, and/or, assist prosecutorial staff in developing briefs and cross examination in formal cases on an as needed basis.

June 2004 to July 2012: Bureau of Technical Utility Services, Finance Division, Pennsylvania Public Utility Commission, Harrisburg, Pennsylvania.

Rate Case Review Specialist/Fixed Utility Financial Analyst:

- Analyzes complex financial, accounting and economic data submitted by gas, electric, water, sewer, pipeline, telephone and other fixed utilities operating in the Commonwealth relative to rate requests, securities, taxes, cost of capital and affiliated interests.

- Writes draft Commission Orders and Reports for securities registration, mergers and change of control applications and affiliated interest agreements.
- Write detail reports (white papers) on financial matters as they relate to regulatory policy.
- Provide financial analysis and advice to other bureaus such as Audits, Law, and the Office of Administrative Law Judge related to financial transactions, utility financing and credit ratings, cost of capital and corporate structure.
- Monitor credit ratings of large electric, gas, telephone, and other foxed utilities operating in Pennsylvania.

EDUCATION

Master of Business Administration (MBA), Indiana University of Pennsylvania 05/1984
Bachelor of Science in Food and Nutrition, Indiana University of Pennsylvania 05/1979

Other Relevant Training:

- PAPUC Emerging Leaders Program January 2012 through June 2012
- SNL Center for Financial Education, Atlanta, GA, *Essentials of Utility Finance*, October 18-19, 2010
- Institute of Public Utilities - Michigan State University, *Water Rate Case School*, May 10-14, 2010
- SNL Center for Financial Education, Stamford, CT, *Analyst Training in the Power and Gas Sector*, December 7-8, 2009.
- The Society of Utility and Regulatory Financial Analysts, *39th Financial Forum – Equity Risk Premium Workbook*, April 19-20, 2007
- PGS Energy Training, Harrisburg, PA, *Fundamentals of Energy/Electricity Futures, Options & Derivatives*, September 23, 2006

Previous Work Experience:

November 2003 to June 2004: Pennsylvania Department of Banking, Harrisburg, Pennsylvania.

Associate Financial Institution Examiner

- Examine financial depository institutions to ensure compliance with established laws, regulations and sound business practices.
- Analyze and rate financial institutions earnings, capital, assets/liabilities, investments, operations and management to determine its overall fiscal health.

March 1998 to May 2003: Wholesale Services, GTE Telephone Operations/Verizon Communications, Harrisburg, Pennsylvania.

Account Manager - Wholesale Services

- Manage complex business relationship between Verizon and 5 large Competitive Local Exchange Carriers and Local Exchange Carriers doing business in PA, VA and WV. Total revenue - $10 Million.
- Sell strategic products such as high capacity DS-1s, DS-3s and Sonet Services. Negotiate service contracts for Operator Services, Directory Assistance Services and CNAM/LIDB Services.
- Manage inter-company relations with approximately 30 other Local Exchange Carriers in the state of Pennsylvania to advocate company policy positions within the telephone industry.
- Insure accuracy of financial settlements exceeding $6 Million between GTE and other Local Exchange Carriers.
- Participate in various PA Telephone Association committees and in industry forums such as North American Numbering Plan Administration (NANPA).

February 1992 to March 1998: GTE Telephone Operations (HQ), Irving, Texas.

Staff Manager - Access Pricing

- Calculate special and switched access prices in 41 jurisdictions for Federal Price Cap and other FCC access price filings. Revenue stream for GTE telephone operations exceeded $4 Billion.
- Provide cost support for specific state and federal special access product filings.

Staff Accountant - Regulatory Accounting

- Prepare financial monitoring reports by state jurisdiction as required by the state Public Utility Commissions for the states KY, SC, OH and HI.
- Prepare financial statements and determine revenue requirements for various rate case proceedings.
- Team member of Gold Team award winner for work on the Hawaii Rate Case (GTE awarded $28M by commission). Also team member for $31M high cost fund award to Contel California, a GTE subsidiary.

Budget Analyst - Domestic Budget

- Produce consolidated financial statements including contribution statements, balance sheet and cash flow statements and other supporting schedules for annual budget and monthly outlook.

October 1986 to February 1992: GTE South Company, Durham North Carolina

Budget Analyst - Sales Administration

- Analyze revenues and margins by product line such as Key systems, PBX systems for the South Area Business Sales organization.
- Calculate incentive compensation payout for 30 individual Account Executives and 5 Regional Sales Managers and 2 Area Sales Managers.

Staff Accountant - Accounting Operations Capital Recovery

- Proper accounting of $180M in annual depreciation/amortization expense, monthly forecast of depreciation and amortization expense, and monthly analysis of depreciation reserve activity.
- Maintain and update accounting and mortality data for annual FCC and State PUC capital recovery studies. Gross Plant investment exceeded $2B.
- Supervised 2 Management and 1 clerical employee.

October 1986 to February 1992: Ogden/Allied Service Corporation, New York, New York

Staff Accountant - General Accounting

- Contribution analysis by operating segments, analysis of general and administrative expenses, capital budget analysis of new business projects, monthly general ledger closings, allocation of operational overheads, and special projects as assigned by the VP of Finance.

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

	)	
County of Dauphin, Pennsylvania	)	**ss**
	)	

AFFIDAVIT OF WITNESS

DAVID L. HUFF, having being first sworn, deposes and says that the statements and exhibits attached hereto were prepared and reviewed by him, and are true and correct to the best of his knowledge and belief.

David L. Huff

SUBSCRIBED AND SWORN BEFORE ME

THIS 30 th day of November, 2016

Victoria R. Moore

Notary Public
(SEAL)

COMMONWEALTH OF PENNSYLVANIA
NOTARIAL SEAL
VICTORIA R. MOORE, Notary Public
City of Harrisburg, Dauphin County
My Commission Expires September 3, 2018

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