

100 FERC 61, 292  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;  
William L. Massey, Linda Breathitt,  
and Nora Mead Brownell.

Midwest Independent Transmission System,                      Docket No. ER02-485-000  
Operator, Inc.

ORDER AFFIRMING INITIAL DECISION, WITH MODIFICATION

(Issued September 23, 2002)

1. This proceeding is before the Commission on exceptions to an Initial Decision issued on April 25, 2002<sup>1</sup> (Initial Decision), regarding the return on common equity (ROE) component for the formula calculation of the transmission service rates for the Midwest Independent Transmission System Operator, Inc. (Midwest ISO) rate zones for participating Midwest ISO transmission owners (Midwest ISO TOs).<sup>2</sup> As discussed below, we will affirm the Initial Decision on all excepted issues. However, as explained further below, we will make an upward adjustment to the ROE set forth in the Initial

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<sup>1</sup>99 FERC ¶ 63,011 (2002).

<sup>2</sup>The Midwest ISO TOs who participated in the filing include: Alliant Energy Corporate Services, Inc., as agent for IES Utilities, Inc. and Interstate Power Co.; Central Illinois Light Co.; Cinergy Services, Inc. (for Cincinnati Gas & Electric Co., PSI Energy, Inc. and Union Light Heat & Power Co.); City Water, Light & Power (Springfield, IL); Hoosier Energy Rural Electric Cooperative, Inc.; Indianapolis Power & Light Company; International Transmission Company; LG&E Corporation (for Louisville Gas and Electric Co. and Kentucky Utilities Co.); Minnesota Power (and its subsidiary Superior Water, L&P); Montana-Dakota Utilities Co.; Minnesota Power (and its subsidiary Superior Water, L&P); Montana-Dakota Utilities Co.; Northwestern Wisconsin Electric Company; Otter Tail Power Company; Southern Illinois Power Cooperative; Southern Indiana Gas & Electric Company; UtiliCorp United, Inc.; and Northern States Power Company and Northern States Power Company (Wisconsin), subsidiaries of Xcel Energy, Inc.

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Decision, and thus, set the ROE for the Midwest ISO TOs at 12.88 percent.

2. Our actions herein advance the public interest by ensuring that Midwest ISO TOs receive appropriate revenues, which will thereby allow the Midwest ISO to bring to customers in the midwestern United States the benefits of a regional transmission organization (RTO).

### **Background**

3. On December 3, 2001, pursuant to section 205 of the Federal Power Act,<sup>3</sup> the Midwest ISO filed proposed revisions to its Open Access Transmission Tariff (OATT), in order to, among other things, increase the ROE from 10.5 to 13 percent for all Midwest ISO pricing zones, except one.<sup>4</sup> The Commission found that the parties raised issues of material fact regarding the 13 percent ROE proposal and therefore, by order issued January 30, 2002<sup>5</sup> (January 30 Order), the Commission accepted and suspended the proposed ROE for a nominal period to become effective, subject to refund, on February 1, 2002, and established expedited hearing procedures.

4. The hearing was held on March 21 and 22, 2002. As stated above, the Initial Decision was issued on April 25, 2002.

5. Briefs on Exceptions and Briefs Opposing Exceptions were filed by the Midwest ISO TOs, the Intervenor Group,<sup>6</sup> and Trial Staff. The Kentucky Public Service Commission, Iowa Utilities Board, Iowa Office of Consumer Advocate, Indiana Office of Utility Consumer Counselor, Missouri Office of the Public Counsel and Minnesota Department of Commerce (collectively, state commissions and state advocates) jointly filed a brief opposing exceptions and incorporating the exceptions submitted by Trial Staff.

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<sup>3</sup>16 U.S.C. § 824(d) (1994).

<sup>4</sup>American Transmission Company, LLC did not join in the filing.

<sup>5</sup>98 FERC ¶ 61,064 (2002); reh'g denied, 98 FERC ¶ 61,356 (2002) (Rehearing Order).

<sup>6</sup>The Intervenor Group includes: American Municipal Power - Ohio; the Coalition of Midwest Transmission Customers and Industrial Energy Users - Ohio; Dairyland Power Cooperative; and the Midwest TDUs.

6. In addition, the Midwest TDUs, a member of the Intervenor Group, filed a non-argumentative motion to lodge, in order to call attention to two recent Commission opinions<sup>7</sup> that the Midwest TDUs believes are relevant to this proceeding. The Midwest ISO TOs filed an opposition to the Midwest TDU's motion to lodge, urging the Commission to reject it as irrelevant.

### **Procedural Matters**

7. As an initial matter, we will accept the Midwest ISO TDU's motion to lodge, as it merely calls to our attention recent orders, without setting forth arguments interpreting those orders.<sup>8</sup>

### **Discussion**

8. The Initial Decision addresses the appropriate ROE for the Midwest ISO TOs. The related litigated issues are fully addressed in the Initial Decision. In the discussion below, we focus on the contested issues raised by the parties' exceptions.

#### **A. Proxy Group**

##### ***Initial Decision***

9. In the Initial Decision, the judge determined that the discounted cash flow (DCF) analysis of one proxy group, proffered by the Midwest ISO TOs, consisting of nine Midwest ISO TOs or parent corporations of the Midwest ISO with publicly-traded common stocks (inclusive of generation and other non-transmission activities)<sup>9</sup> was the appropriate proxy group for use in determining the ROE for the Midwest ISO TOs. The judge first noted that since the transmission assets of the Midwest ISO are owned by 21 different entities, which do not have publicly-traded stock, it is difficult to determine the

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<sup>7</sup>UtiliCorp United, Inc., 99 FERC ¶ 61,280 (2002) and Midwest Independent Transmission System Operator, Inc., 99 FERC ¶ 61,258 (2002).

<sup>8</sup>Duke/Louis Dreyfus L.L.C., et al., 75 FERC ¶ 61,261 (1996).

<sup>9</sup>The Midwest ISO TO proxy group includes: Allete, Inc.; Alliant Energy; CInergy Corp.; DTE Energy Co.; MDU Resources Group; Otter Tail Corp.; Utilicorp United, Inc.; Vectren Corp.; and Xcel Energy, Inc.

ROE for those entities. The judge further noted that there are no publicly-traded, independent, pure electric transmission companies to be used as benchmarks to estimate a ROE for the Midwest ISO transmission system. Therefore, the judge found that one way to determine the ROE for the Midwest ISO TOs is to develop a zone of reasonable returns for a proxy group of companies having analogous risks. The judge reasoned that the Midwest ISO TO proxy group was the best proxy group, since it involves companies that are currently in the Midwest ISO, and includes comparable risk companies that are similar in profiles and size. The judge rejected DCF analyses using other proxy groups, including: (1) natural gas pipeline transmission operators, based upon Commission precedent in SoCal<sup>10</sup>; (2) Moody's electric utilities and Standard and Poor's electric utilities, based upon Commission precedent in Systems Energy<sup>11</sup>; and (3) generation-divested electric utilities, because they consisted of distribution, not transmission, companies.<sup>12</sup>

### **Exceptions and Opposing Exceptions**

10. The Intervenor Group takes exception to the judge's reliance upon the Midwest ISO TO proxy group. Having proffered a proxy group consisting of generation-divested electric utilities (generation-divested proxy group), the Intervenor Group contends that the judge failed to adequately explain her reasons for rejecting that group. The Intervenor Group states that, contrary to the judge's finding, the generation-divested proxy group owns both transmission and distribution. Moreover, the Intervenor Group contends that the Midwest ISO TO proxy group is not a reliable proxy group for setting the ROE at issue here, since, according to the Intervenor Group, the Midwest ISO TOs in that group engage in significant non-wires businesses, such as energy marketing, and non-electric businesses, such as telecommunications and used car sales. The Intervenor Group states that the risks and growth expectations for every Midwest ISO TO company is dominated by non-transmission operations. The Intervenor Group argues that between the Midwest ISO TO proxy group and the generation-divested proxy group, the business of the latter group is less-diversified and more closely resembles the transmission business for which the ROE is being set.

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<sup>10</sup>Southern California Edison, 92 FERC ¶ 61,070 (2000); reh'g pending (SoCal).

<sup>11</sup>Systems Energy Resources, Inc., 92 FERC ¶ 61,119 (2000), reh'g denied, 96 FERC ¶ 61,165 (2002) (Systems Energy).

<sup>12</sup>Initial Decision at 7-11.

11. Trial Staff and the Midwest ISO TOs argue that in relying upon the Midwest ISO TO proxy group, the judge correctly followed Commission precedent in SoCal. Trial Staff also states that the judge appropriately determined that the evidence that transmission facilities investments are less risky than other investments of electric utilities was too speculative.

### **Commission Response**

12. Our review of the judge's reasoning and the underlying record, as well as the parties' arguments on and opposing exceptions, leads us to summarily affirm the judge's finding that the proxy group proffered by the Midwest ISO TOs is the appropriate proxy group for use in determining the ROE for the Midwest ISO TOs. The Intervenor Group has not demonstrated that the group is unrepresentative of the Midwest ISO TOs. We are unpersuaded by the Intervenor Group's arguments that the generation-divest proxy group more closely resembles the transmission business for which the ROE is being set and that transmission investments are less risky than the other investments of the Midwest ISO TO proxy companies. For the reasons set forth in the Initial Decisions, we find that the Intervenor Group has failed to set forth convincing evidence in either regard.

## **B. Discounted Cash Flow Analysis**

### **1. Estimation Period**

#### **Initial Decision**

13. In calculating the zone of reasonable returns for the Midwest ISO TO proxy group, the judge adopted the one-step, constant growth DCF model set forth in SoCal.<sup>13</sup> As part of the DCF analysis, the judge calculated sustainable growth rates, " $br + sv$ ,"

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<sup>13</sup>92 FERC at 61,262-63. DCF methodology determines the ROE by summing the dividend yield (with an adjustment for the quarterly payment of dividends) and expected growth rate. The resulting formula is  $D/P (1+.5g)+g=k$ , where "D/P" is the dividend yield, "g" is the sustainable growth rate of dividends per share, and "k" is the resulting ROE. The sustainable growth rate is calculated by the formula:  $G=br+sv$ , where "b" is the expected retention ratio, "r" is the expected earned rate of ROE, "s" is the percent of common equity expected to be issued annually as new common stock, and "v" is the equity accretion rate.

based upon Value Line data for years 2001, 2002 and 2004-2006, and averaged all three rates. The judge found that using three estimates or a five-year estimation period provides a more adequate and reliable estimate of the sustainable growth rate to be used as the "br" element of the DCF formula. In addition, the judge found this approach to be consistent with SoCal, in which the Commission calculated the projected "b x r" growth rate by averaging three Value Line Estimates. The judge found that, despite the historical label attached by some parties, the 2001 data were largely projections and therefore relevant.<sup>14</sup>

### ***Exceptions and Opposing Exceptions***

14. The Midwest ISO TOs contend that the Value Line 2001 data should have been omitted from the judge's calculations. First, noting that sustainable growth rates are to be based on projections, they argue that the Value Line 2001 data were outdated by March 2002, when the Midwest ISO TOs' witness filed his rebuttal testimony and updated his DCF calculations for the Midwest ISO TO proxy group. Second, the Midwest ISO TOs disagree with the use of Value Line's projections for 2001, noting that the ROE at issue here is to be effective February 1, 2002. Thus, the Midwest ISO TOs argue that the judge's calculations are contrary to SoCal. In that case, the Commission used only forward-looking Value Line data. Finally, they argue that the 2001 data skews the DCF analysis, because, for example, Value Line changed its retention ratio projection for one company in the Midwest ISO TO proxy group (DTE Energy) between 2001 and 2002 data.

15. Trial Staff asserts that, contrary to the Midwest ISO TOs' contention, as of March 2002, almost all the Value Line 2001 data required to derive a growth estimate were still projections. In support of the judge's ruling, Trial Staff states that seven of the nine proxy companies had not yet reported all of the data required to calculate a sustainable growth rate for the Midwest ISO TO proxy companies, with Value Line sheets dated January 4, 2002,<sup>15</sup> and that therefore the judge's calculations were based on projected data, even up to March 13, 2002. With regard to the change in the proposed retention ratio of one of the Midwest ISO TO proxy companies, Trial Staff argues that changes in one projection or another will always occur, sometimes in favor of one part and

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<sup>14</sup>Initial Decision at 16.

<sup>15</sup>Trial Staff states that this is evidenced by the fact that much of the data in the Value Line sheets was in boldface, which Value Line uses to indicate projections, as opposed to regular typeface, which Value Line uses to indicate reported numbers.

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sometimes in favor of another. Accordingly, Trial Staff contends that this is no reason to reject the judge's reliance on Value Line's 2001 data.

16. The Intervenor Group also disputes the Midwest ISO TOs argument. The Intervenor Group posits that the Value Line 2001 data project how the earnings-per-share and other results for 2001 would turn out upon the publishing of company annual reports. They contend that Value Line 2001 data do not reflect actual results. The Intervenor Group also points out that use of the Value Line reports provide three forward-looking growth projections, one for each of the next two reporting years for which actual data is not yet available, 2001 and 2002, and one for a medium-term, three year future window centered on 2005, which is consistent with SoCal. The Intervenor Group further argues that ignoring the 2001 data would distort the SoCal DCF methodology, since the medium-term projection is given one-third weighting in the calculation, with a two-third weighting given to the shorter term projections.

### **Commission Response**

17. We affirm that the judge's use of Value Line data for 2001, 2002 and 2004-2006 (three estimates or a five-year estimation period) is appropriate and consistent with SoCal. The Midwest ISO TOs have failed to demonstrate that the judge erred in following the SoCal methodology. Moreover, as noted by Trial Staff, most of the data on the Value Line sheets are in boldface type, which Value Line uses to indicate projections. In addition, the judge acknowledged that except for two companies, the Value Line 2001 data is predominately forward-looking growth projection data, and not historical data. Accordingly, we find that the judge's use of the Value Line 2001 data as the first estimation year in a one-step, constant growth DCF analysis to calculate "g," the sustainable growth rate of dividends per share, was proper.

## **2. Dividend Yield**

### **Initial Decision**

18. As part of the DCF analysis, the judge also determined the correct way in which to calculate the estimated low and high ROE for each company in the Midwest ISO TO proxy group. She calculated the estimated low ROE for each company by adding the adjusted average low dividend yield to the lower of the two growth rates already derived (one derived from Value Line data and one from the Institutional Brokers Estimate Service (IBES)). The judge then calculated the estimated high ROE for each company

by adding the adjusted average high dividend yield to the higher of the two growth rates. The judge found this approach to be consistent with SoCal.<sup>16</sup>

### ***Exceptions and Opposing Exceptions***

19. Trial Staff<sup>17</sup> acknowledges that the judge's calculations for high and low ROE for the Midwest ISO TO proxy companies follows the method used in SoCal. However, Trial Staff argues that the better approach, which should be utilized here, is to add the low dividend yield to the higher growth rate, and the high dividend yield to the lower growth rate. As Trial Staff explains, to the extent a company pays out a relatively small percentage of its earnings in dividends, its future growth in dividends will be enhanced, and to the extent a company pays out a relatively high percentage of its earnings in dividends, its future growth in dividends will be dampened. Trial Staff asserts that the Commission acknowledged the truth of this logic in SoCal,<sup>18</sup> when it found that "[t]he higher payout ratios attributable to electric utilities cause these companies to have significantly lower expected dividend growth rates than most other industrial companies . . ." Trial Staff states that while its suggested approach differs from the approach the Commission took in SoCal in deriving a zone of reasonableness, it is consistent with the Commission's reasoning in that case.

20. On the other hand, the Midwest ISO TOs support the judge's reliance upon SoCal, and state that the Commission should continue to employ the methodology set forth in that case.

### ***Commission Response***

21. We are not persuaded by Trial Staff's suggestion to modify the calculation of the dividend yield, which would alter the zone of reasonableness. Consistent with SoCal,

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<sup>16</sup>Initial Decision at 13-14.

<sup>17</sup>For purposes of discussion of the dividend yield, "Trial Staff" shall refer to both Trial Staff and the state commissions and state advocates.

<sup>18</sup>92 FERC at 61,262.

Consumers Energy,<sup>19</sup> and Systems Energy, we find that the judge used a proper methodology in determining the estimated low and high ROE for each company in the Midwest ISO TO proxy group.

**C. Setting the ROE at the Midpoint Within the Zone of Reasonableness**

22. After calculating the zone of reasonableness for the ROE, based upon the range of the estimated lowest and highest ROEs for each of the Midwest ISO TO proxy companies,<sup>20</sup> the judge specified that the midpoint of that range, or 12.38 percent, reflected the appropriate ROE for Midwest ISO TOs. The judge found that using the midpoint as the ROE is consistent with SoCal, Consumers Energy, and Systems Energy, in which the Commission found that using the midpoint of the zone of reasonableness resulted in a reasonable ROE.<sup>21</sup> The judge rejected Trial Staff's recommendation to use the average. The judge cited Canadian Ass'n of Petroleum Producers v. FERC,<sup>22</sup> where the court stated that the "midpoint doesn't completely disregard the middle three numbers; the highest and lowest numbers achieve their status by reference to all five numbers."

23. The judge further rejected arguments in favor of adjusting the ROE toward the upper half of the zone of reasonableness and arguments in favor of adjusting the ROE toward the lower half of the zone of reasonableness. The judge found that, contrary to the Midwest ISO TOs assertion, a comparison of the bond ratings of the Midwest ISO and Midwest ISO TO proxy companies did not warrant setting the ROE in the top half of the zone of reasonableness, because the Midwest ISO TO proxy companies have a higher bond rating than the Midwest ISO and therefore are less risky than the Midwest ISO.<sup>23</sup> The judge determined that the midpoint of the Midwest ISO TO proxy group properly reflects the possible risks the Midwest ISO TOs may face. The judge further rejected, as

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<sup>19</sup>Consumers Energy Co., 98 FERC ¶ 61,333 (2002) (Consumers Energy).

<sup>20</sup>As set forth in Appendix A to the Initial Decision, Alliant had the lowest estimated ROE of 8.79 percent and UtiliCorp had the highest estimated ROE of 15.96 percent.

<sup>21</sup>Initial Decision at 25.

<sup>22</sup>254 F.3d 289, 298 (D.C. Cir. 2001).

<sup>23</sup>The judge cited SoCal, 92 FERC at 61,266.

outside the scope of the proceeding, the Midwest ISO TOs argument that an upper-end ROE may be supported as an innovative rate. The judge noted that in the Rehearing Order, the Commission held that innovative rates must be submitted to the stakeholder process prior to submitting them for filing. The judge also refused to set the ROE in the lower half of the zone of reasonableness, as the Intervenor Group had suggested, based upon the finding that current Commission policy utilizes the midpoint to set the ROE for electric utilities.

### **Exceptions and Opposing Exceptions**

24. The Intervenor Group and Trial Staff<sup>24</sup> argue that the average is the most preferable measure, rather than the midpoint, in setting the ROE.<sup>25</sup> They assert that the midpoint gives consideration only to the two most extreme values in a proxy group, the lowest estimated ROE of one company and the highest estimated ROE of a second company. Moreover, the Intervenor Group argues that the highest estimated ROE in the Midwest ISO TO proxy group (15.96 percent), for UtiliCorp (now, Aquila), is derived from UtiliCorp's energy marketing unit, not its transmission business and therefore is inappropriate.

25. Trial Staff concedes that historically, the Commission has relied upon the midpoint in electric cases. However, Trial Staff and the Intervenor Group argue that the Commission has relied upon the median in setting the ROE for gas pipelines, and that there is no reason to proceed differently with regard to electric utilities.

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<sup>24</sup>For purposes of discussion of the midpoint, "Trial Staff" shall refer to both Trial Staff and the state commissions and state advocates.

<sup>25</sup>The midpoint of all the estimates of return of a proxy group is the average of the highest and lowest estimated returns of all members of the group. The median is that point within the zone of reasonableness where half the returns have a higher value and half the returns have a lower value. The average is the sum of all the high and low estimates of each member of the proxy group, divided by the number of estimates. Trial Staff Brief on Exceptions at 7.

26. The Midwest ISO TOs argue that while the midpoint is the appropriate starting place, the ROE should be set above the midpoint to best satisfy the demonstrated investor expectations for returns on energy transmission investments,<sup>26</sup> fully reflect the risks of participating in the Midwest ISO,<sup>27</sup> facilitate the Midwest ISO's continued expansion, and ensure that the transmission sector attracts sufficient capital. The Midwest ISO TOs take issue with the judge's interpretation of SoCal,<sup>28</sup> and argue that in that case, the Commission found that a return in the upper half of the zone was necessary, because the utility faced additional risks by turning over control of its transmission assets to the California ISO. They contend that the same reasoning should apply here. The Midwest ISO TOs further assert that in setting the proposed 13 percent ROE for hearing, members of the Commission indicated that the level of gas transmission ROEs could be a useful reference for the electric ROE in this case.<sup>29</sup> Accordingly, the Midwest ISO TOs state the proposed 13 percent ROE should be accepted.

27. On the other hand, the Intervenor Group argues that neither cost-based considerations, nor incentive considerations, support placing the ROE above the center of the zone of reasonableness. Indeed, the Intervenor Group argues that the judge should have adjusted the ROE to a point in the lower half of the identified zone of reasonableness. The Intervenor Group argues that the investments in transmission operated by the Midwest ISO are less risky than the Midwest ISO TOs' business taken as a whole,<sup>30</sup> and less risky than the central risk of an expanded set of proxies that includes

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<sup>26</sup>The Midwest ISO TOs contend that their witness' gas transmission DCF analysis found that equity investors in the typical gas transmission company expect to earn the same ROE requested in this case for restructured electric transmission, i.e., 13 percent.

<sup>27</sup>According to the Midwest ISO TOs, these risks include cost increases, including payment of the Midwest ISO Schedule 10 administrative charge and other costs such as congestion uplift and payments to generators; revenue reductions from loss of pancaked rates; loss of control of transmission assets; loss of section 205 filing rights Midwest ISO TOs Brief On Exceptions at 23.

<sup>28</sup>92 FERC at 61,266-67.

<sup>29</sup>The Midwest ISO TOs cite Federal Energy Regulatory Commission, 783rd Regular Meeting, Open Meeting (January 30, 2002), Tr. at pp. 41-43.

<sup>30</sup>The Intervenor Group further explains that this is because the Midwest ISO TO  
(continued...)

both the market-participant Midwest ISO TOs and more representative wires-only companies. Accordingly, argue the Intervenor Group, the ROE for the Midwest ISO TOs should be adjusted toward the lower half of reasonable range.

28. Trial Staff maintains that the record supports neither the proposed 13 percent ROE, nor a ROE set in the lower half of the identified zone of reasonableness. Trial Staff states that in arguing for a higher ROE, the Midwest ISO TOs failed to demonstrate that investors expect higher returns on transmission investments and relied upon an inapt analysis of the gas pipeline industry. In addition, Trial Staff states that the Midwest ISO TO's reliance upon the Commissioners' comments at the March 27 meeting is inappropriate, because at the time the Commissioners made those comments, they had heard only from the Midwest ISO TOs and in any case, had decided to send to hearing the issues upon which they were commenting. In addition, Trial Staff contend that, contrary to the Midwest ISO TOs position, the judge correctly interpreted and relied upon SoCal. Trial Staff states that in SoCal, the Commission rejected as too speculative an argument substantially similar to the argument proffered by the Midwest ISO TOs here, namely, that transmission owners face increased risks by joining an ISO or RTO.

29. The state commissions and state advocates also contend that the Midwest ISOs failed to provide any evidence that transferring operational control will increase operational risks. They assert that the risk of retail cost recovery does not justify a ROE of 13 percent.

### **Commission Response**

30. Our review of the presiding judge's reasoning and the underlying record, as well as the parties' arguments on and opposing exceptions, leads us to summarily affirm the presiding judge's finding that the midpoint of the zone of reasonableness represents the appropriate ROE in this case. The Commission has consistently used the midpoint in setting the ROE for electric utilities,<sup>31</sup> and we see no reason to depart from our precedent here. We are unpersuaded by appeals to use the methodology utilized in setting the ROE

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<sup>30</sup>(...continued)

proxy companies are not solely engaged in the transmission business and that the investments of the Midwest ISO TO parent companies in transmission operated by the Midwest ISO are substantially safer than investments in non-transmission-related investments in power marketing, used-car sales, and telecommunications.

<sup>31</sup>See Consumers Energy, 98 FERC at 62,416; SoCal, 92 FERC at 61,266.

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for gas pipelines, for we have also consistently emphasized that significant differences exist between the electric and gas industries.<sup>32</sup> Furthermore, we reject the Intervenor Group's argument that UtiliCorp's inclusion in the Midwest ISO TO proxy group improperly skews the midpoint upward. As we previously stated, we find that the Midwest ISO TO proxy companies properly represent the Midwest ISO TOs, for the reasons set forth in the Initial Decision.

31. As summarized above, certain parties argue that, even if the midpoint (as opposed to the average or median) of the range of reasonableness is to be used in determining the ROE, then the ROE should be adjusted either up or down within that range. We disagree. We find that, in refusing an upward adjustment to the ROE, the judge properly rejected arguments concerning the riskiness of an utility transferring its transmission assets to an RTO. We further find that the judge properly refused a downward adjustment to the ROE for the reasons set forth in the Initial Decision. There are, however, policy reasons to make upward adjustments -- particularly with regard to the level of operational independence that the Midwest ISO provides. In this case, we will make an upward adjustment of 50 basis points from the proxy group midpoint for the turning over of operational control of transmission facilities. We will consider providing additional upward adjustments for greater levels of independence. The Commission will be clarifying its incentive rate policy in the near future with concrete statements of the behavior and performance we wish to incentivize.

The Commission orders:

The Initial Decision in this proceeding is hereby affirmed, with modification, as discussed in the body of this order.

By the Commission.

( S E A L )

Linwood A. Watson, Jr.,  
Deputy Secretary.

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<sup>32</sup>See Consumers Energy, 98 FERC at 61,261-62; Systems Energy, 92 FERC at 61,443-45.

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