

**PUBLIC VERSION 118 FERC ¶ 63, 024**  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

New Dominion Energy Cooperative  
Old Dominion Electric Cooperative

Docket No. ER05-18-002  
Docket No. ER05-309-002

INITIAL DECISION

(Issued February 5, 2007)

**Appearances**

*Adrienne Clair, Esq., John Pirko, Esq.*, for Old Dominion Electric Cooperative and New Dominion Energy Cooperative.

*Alan Robbins, Esq., Debra Roby, Esq., Alyssa Schindler, Esq.*, for Northern Virginia Electric Cooperative.

*Gopal Swaminathan, Esq., Lorna Hadlock, Esq.*, for the Federal Energy Regulatory Commission.

JUDITH A. DOWD, Presiding Administrative Law Judge

**I. Background and Procedural History**

1. Historically, Old Dominion Electric Cooperative (Old Dominion), a not-for-profit public utility, provided generation, transmission, ancillary, and related services to its twelve member electric distribution cooperatives (Member Cooperatives, or Members).<sup>1</sup> The Members, which serve retail customers in Virginia, Maryland, Delaware, and West Virginia, collectively owned Old Dominion. Old Dominion was a party to a Wholesale

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<sup>1</sup> The Member Cooperatives are: A&N Electric Cooperative; BARC Electric Cooperative; Community Electric Cooperative; Choptank Electric Cooperative; Delaware Electric Cooperative; Mecklenburg Electric Cooperative; Northern Neck Electric Cooperative; Northern Virginia Electric Cooperative (NOVEC); Prince George Electric Cooperative; Rappahannock Electric Cooperative (REC); Shenandoah Valley Electric Cooperative; and Southside Electric Cooperative.

Power Contract (WPC) with each Member Cooperative. Under the WPCs, the Members purchased substantially all of their power requirements from Old Dominion at cost-based rates regulated under a cost-of-service formula accepted by the Federal Energy Regulatory Commission (the Commission or FERC).

2. In July 2004, the Member Cooperatives unanimously agreed to reorganize Old Dominion. The terms of the reorganization provided for the creation of a new entity—New Dominion Energy Cooperative (New Dominion). The expectation was that New Dominion would become the sole member of Old Dominion, would purchase all of the output and services produced by Old Dominion's electric facilities, and would take responsibility for the transmission and market functions formerly provided by Old Dominion, including provision of electric service to the Member Cooperatives under the WPCs. The Member Cooperatives would withdraw as members of Old Dominion and in lieu receive membership interests in New Dominion. To implement the reorganization, Old Dominion and New Dominion (collectively, Applicants) made a series of filings with the Commission in October and December of 2004. Two of those filings are at issue in this proceeding and are summarized as follows.

3. On October 5, 2004, as amended on January 7, 2005, in Docket No. ER05-18-000, Applicants filed an application seeking re-approval of the rate schedule and formula rate currently on file for Old Dominion for use by New Dominion (New Dominion Tariff). The filing included several changes to the general terms of the tariff to allow for changed circumstances, including the change in corporate identity, the assignment of the WPCs from Old Dominion to New Dominion, and the inclusion of Old Dominion and New Dominion in the PJM Interconnection, L.L.C. (PJM). On December 7, 2004, as amended on February 4, 2005, Old Dominion filed, in Docket No. ER05-309-000, a new tariff for its sales to New Dominion (Old Dominion Tariff) and a notice of cancellation for its existing tariff on file with the Commission. The new tariff includes a formula for allocating costs between demand-related and energy-related expenses for the purposes of billing such costs to New Dominion.<sup>2</sup>

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<sup>2</sup> Applicants also made the following filings with the Commission, none of which are at issue in this proceeding. On October 5, 2004, as amended on January 7, 2005, New Dominion requested authority to sell energy and capacity to third parties and to the Member Cooperatives at market-based rates (Docket No. ER05-20-000). Also on October 5, 2004, as amended January 7, 2005, Applicants filed a joint application under section 203 of the Federal Power Act (FPA), 16 U.S.C. § 824b (2000), requesting Commission authorization to assign Old Dominion's existing WPCs with the Member Cooperatives to New Dominion (Docket Nos. EC05-1-000 and EC05-1-001). In the EC05-1 docket, an issue as to whether the proposed transaction may have an adverse impact on rates was set for hearing. *Old Dominion Elec. Coop.*, 110 FERC ¶ 61,274 at P 2 (2005). On October 12, 2004, Applicants filed an application under section 204 of the FPA, 16 U.S.C. § 824c (2000), seeking authorization to guarantee each other's

4. On March 8, 2005, the Commission issued an Order Accepting for Filing and Suspending Tariff Revisions and Establishing Hearing and Settlement Judge Procedures, Granting Market-Based Rate Authority and Authorizing Issuance of Securities (*i.e.* the March 8 Order *supra* n.2). In the March 8 Order, the Commission found that Applicants' filings in Docket Nos. ER05-18-000 and ER05-309-000 may be unjust, unreasonable, unduly discriminatory or preferential or otherwise unlawful. The Commission granted the motions to intervene of the Virginia State Corporation Commission (VSCC), Bear Island Paper Company, L.P. (Bear Island),<sup>3</sup> and NOVEC and set Docket Nos. ER05-18-000 and ER05-309-000 for hearing and settlement judge procedures.<sup>4</sup> Additionally, the Commission explicitly found that Applicants' filings are not initial rates.<sup>5</sup>

5. Applicants reached agreement with Bear Island and the VSCC with respect to the issues set for hearing in this proceeding and filed a settlement offer (Settlement) on October 13, 2005. Only NOVEC filed comments opposing the Settlement. Commission Trial Staff and Bear Island filed Initial and Reply Comments supporting the Settlement, and the VSCC and the Applicants filed supporting Reply Comments. The Commission approved the Settlement without modification on April 7, 2006.<sup>6</sup> The Settlement makes certain changes to the tariffs for cost-based sales from Old Dominion to New Dominion and from New Dominion to the Member Cooperatives, as they were filed in these dockets.<sup>7</sup> The Settlement changes the classification for Account 553 from energy-related to demand-related<sup>8</sup> and provides for Applicants and Bear Island to enter a Demand Side Management Services Agreement (DSM Agreement), which is attached to the

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obligations and for New Dominion to issue and renew short-term debt (Docket Nos. ES05-5-000, ES05-6-000, and ES05-7-000). Applicants' request to guarantee each other's obligations, as well as New Dominion's requests to issue and renew short-term debt and for market-based rates authority, were granted by Commission order dated March 8, 2005. *New Dominion Energy Coop.*, 110 FERC ¶ 61,275 (2005) (March 8 Order). On February 2, 2006, the undersigned, who was the Presiding Judge in the hearing in Docket Nos. EC05-1-000 and EC05-1-001, issued an Initial Decision finding that Applicants' reorganization will not negatively impact rates. The Initial Decision was adopted by the Commission on December 21, 2006. *Old Dominion Elec. Coop.*, 117 FERC ¶ 61,313 (2006).

<sup>3</sup> Bear Island is a retail customer of Member Cooperative REC.

<sup>4</sup> *New Dominion Energy Coop.*, 110 FERC ¶ 61,275 at P 27.

<sup>5</sup> *New Dominion Energy Coop.*, 110 FERC ¶ 61,275 at n.12.

<sup>6</sup> *New Dominion Energy Coop.*, 115 FERC ¶ 61,025 (2006) (Settlement Order).

<sup>7</sup> See Settlement at § 1.03.

<sup>8</sup> *Id.* at § 1.04.

Settlement.<sup>9</sup> Under the Settlement, New Dominion agrees not to charge the Member Cooperatives market-based rates except with respect to new customers or expansions by existing customers.<sup>10</sup> The tariffs as they were revised by the Settlement are referred to herein as respectively the Old Dominion Settlement Tariff and the New Dominion Settlement Tariff (collectively, Settlement Tariffs), and the rate formulas that apply under the Settlement are referred to herein as the Settlement Rate Formulas. In approving the Settlement, the Commission stated that since NOVEC was not a party to the Settlement it would not be bound by the Settlement terms.<sup>11</sup>

6. Pursuant to the Commission's Settlement Order, a hearing with respect to NOVEC's rate issues in this proceeding was held beginning on October 17, 2006 and continuing through October 19, 2006.<sup>12</sup> Participants in the hearing were Applicants, NOVEC, and Commission Trial Staff (Staff). Each of them filed an Initial Brief on November 17, 2006,<sup>13</sup> and a Reply Brief on December 18, 2006. The following issues are disputed:

- Are Applicants' filings unclear and confusing? If so, are the filings unjust and unreasonable as a result?
- Is the Applicants' allocation of FERC Account No. 553 just and reasonable?
- Is Applicants' market-based rates proposal just and reasonable?
- Is the depreciation methodology proposed by Applicants just and reasonable?
- Are the reactive power charges proposed by Applicants just and reasonable?
- Is the allocation of cost responsibility among New Dominion's members, as proposed by Applicants, just and reasonable?

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<sup>9</sup> *Id.* at § 2.01 and Attachment 2. Under the DSM Agreement, Applicants may curtail Bear Island's demand for 45 days annually from June 1 through September 30, and may limit Bear Island's demand to 24 megawatts (MW), *i.e.* 24,000 kilowatts (kW), for up to five hours per day curtailed. *Id.* at §§ 1.1–1.2. Applicants will bill REC for a monthly billing demand of 24,000 kW. *Id.* at § 3.2.

<sup>10</sup> *Id.* at § 1.01.

<sup>11</sup> *New Dominion Energy Coop.*, 115 FERC ¶ 61,025 at P 12.

<sup>12</sup> *See id.* (“A hearing with respect to NOVEC's rate issues will still be held in this docket.”).

<sup>13</sup> On November 20, 2006, the undersigned Presiding Judge issued an order accepting the non-public version of Applicants' brief, which was filed one day later than the public version and one day out-of-time.

- Is the Applicants' interpretation of the Prior Period Adjustment for Demand Revenues provision of the New Dominion Tariff arbitrary and capricious?
- Should Applicants be required to revise their rate formulas to accommodate prospective changes in NOVEC's WPC?

## II. Discussion of the Issues

### Issue 1: Are the Applicants' filings unclear and confusing? If so, are the filings unjust and unreasonable as a result?

#### A. Positions of the Parties

##### Staff

7. Staff argues that Applicants' filings are unjust and unreasonable for three reasons.<sup>14</sup> Staff contends that: (1) Applicants have not met their burden of proof because they have failed to support their proposal with sufficient record evidence; (2) Applicants' filings are unclear and confusing because Applicants did not enter into evidence a clean version of the New Dominion Tariff and thus "there is no one-to-one correspondence between either: (i) the sheets of the [New Dominion Tariff] and the Old Dominion Tariff; or (ii) the sheets of the [New Dominion Tariff] and the New Dominion Settlement Tariff,"<sup>15</sup> making it difficult to understand the proposed rate changes;<sup>16</sup> and (3) Applicants' proposal to use the Prior Period Adjustment for Demand Revenues provision (PPA Provision) of the New Dominion Tariff to recover under-recoveries associated with implementation of the Settlement is arbitrary and capricious.

##### Applicants

8. Applicants agree with Staff that they bear the initial burden of establishing that their formula rates are just and reasonable.<sup>17</sup> Applicants point out that Staff fails to cite any specific instances where Applicants' burden has not been met.<sup>18</sup> Applicants contend that they have submitted sufficient evidence to show that their rates are just and

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<sup>14</sup> Staff Initial Brief (IB) at 16–17; Staff Reply Brief (RB) at 5–6.

<sup>15</sup> Staff IB at 17; *see also* Staff RB at 6.

<sup>16</sup> Staff IB at 16; Staff RB at 5–6.

<sup>17</sup> Applicants RB at 5.

<sup>18</sup> *Id.*

reasonable. Applicants suggest that the burden of proof is not even relevant except with respect to the reactive power issue.<sup>19</sup>

9. Applicants also dispute Staff's characterization of the filings as unclear and confusing.<sup>20</sup> Applicants note that the only version of the rate formulas not placed into evidence is the clean version of the New Dominion Tariff.<sup>21</sup> Moreover, Applicants maintain that the applications as originally filed include a clean version of the New Dominion Tariff and are public documents.<sup>22</sup> Applicants state that they "saw no reason to unnecessarily burden the hearing record" by marking the applications as exhibits.<sup>23</sup> Applicants ultimately conclude that Staff's confusion over the rate filings "is not a basis for finding that the proposed rate filings are not just and reasonable."<sup>24</sup>

## B. Discussion and Ruling

10. I agree with Applicants that Staff's burden of proof argument lacks specificity. I also agree that the burden of proof is critical only with respect to the reactive power issue. The burden of proof thus will be discussed in detail *infra* P 48–55.

11. The principal basis for Staff's complaint that Applicants' filings are unclear and confusing seems to be that Applicants did not enter into evidence a clean version of the New Dominion Tariff. As Applicants correctly note, however, the application filed in Docket No. ER05-18-000 on October 5, 2004 (October 5 Filing) includes the clean version of the New Dominion Tariff and is a public record.<sup>25</sup> Staff had notice that the filed application is the essence of this litigation. At most Applicants are guilty of harmless error by failing to request that administrative notice of the rate filing be taken. I also note that on December 8, 2004, the Commission's Office of Markets, Tariffs & Rates (OMTR) issued a deficiency letter with respect to the October 5 Filing, seeking additional information to assist OMTR with its analysis of the filing, but sought no

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<sup>19</sup> *See id.* at 6.

<sup>20</sup> *Id.* at 11–14.

<sup>21</sup> *Id.* at 13–14.

<sup>22</sup> *Id.* at 13.

<sup>23</sup> *Id.* at 13–14. Applicants also suggest that the applications should be considered part of the hearing record despite not being marked as exhibits. *See id.* at 14.

<sup>24</sup> *Id.* at 14.

<sup>25</sup> Application for Approval of Assignment of Wholesale Power Contracts, Acceptance of Conforming Changes to Formulary Rate Tariff and Grant of Authority to Make Wholesale Power Sales at Market-Based Rates, Docket Nos. EC05-1-000, ER05-18-000, and ER05-20-000, at Attachment C (October 5, 2004).

additional information or clarification after Applicants' January 7, 2005 amendment to the October 5 Filing. I thus find no merit in Staff's argument that Applicants' filings are unclear and confusing, and I decline to find Applicants' filings unjust and unreasonable on this basis.

12. Staff's objections concerning the PPA Provision focus on Applicants' interpretation of the provision rather than the provision itself, which has been in effect for a number of years. In any event, because the issue Staff raises with respect to the PPA Provision is tied to the issue concerning the DSM Agreement, considered later herein, Applicants' arguments and the discussion and ruling on the PPA Provision issue are discussed fully *infra* Issue 7 (*see infra* P 83–88).

## **Issue 2: Is the Applicants' allocation of FERC Account 553 just and reasonable?**

13. Staff and Applicants both support a classification of Account 553 based on demand.<sup>26</sup> NOVEC argues the classification should be based on energy. Consistent with the arguments of Staff and Applicants, I find that the appropriate classification of Account 553 is demand-related.

### **A. Positions of the Parties**

#### **NOVEC**

14. NOVEC notes that Applicants have not filed with the Commission to amend their initial classification of Account 553 as energy-related in these proceedings.<sup>27</sup> NOVEC

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<sup>26</sup> In its Initial Brief, Staff asserts that the result of Applicants' "hybrid" allocation on the basis of energy in the Old Dominion Tariff and on the basis of demand in the New Dominion Tariff is effectively an allocation of Account 553 entirely on the basis of energy. Staff IB at 19–20. Staff explains that since New Dominion buys all its power from Old Dominion subject to the cost allocations in the Old Dominion Tariff, New Dominion's power purchases from Old Dominion reflect the cost allocations of the Old Dominion Tariff. *Id.* at 20 (citing Ex. ODC-6 at 8:1–11, 9:6–14; Ex. ODC-7; Ex. S-2). Applicants, however, clarify in their Initial Brief that, although their initial application in Docket No. ER05-309 proposed to classify Account 553 as energy (to conform with PJM's method of classification), their view changed prior to the filing of their direct testimony due to discussions with Staff and various parties, and they now fully support a classification based on demand. Applicants IB at 33–34.

<sup>27</sup> NOVEC IB at 22 (citing Tr. at 300). NOVEC also alleges that Applicants improperly rely on settlement discussions to support their change from the classification of Account 553 as originally filed. NOVEC RB at 4 (referring to Applicants IB at 33–34).

cites Rule 205 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.205 (2006), which states that a utility "must make a tariff or rate filing in order to establish or change any specific rate, rate schedule, tariff, tariff schedule, fare, charge, or term or condition of service, or any classification, contract, practice, or any related regulation established by and for the applicant."<sup>28</sup> According to NOVEC, Applicants' decision not to file an amendment with the Commission was "a fatal legal decision."<sup>29</sup>

15. Additionally, NOVEC maintains that reclassification of Account 553 from energy- to demand-related will increase NOVEC's rates.<sup>30</sup> NOVEC Witness Paul A. Arsuaga (NOVEC Witness Arsuaga) explains:

[Retail customer] Bear Island's total annual delivered kW demands are approximately 1.5 percent of the total Old Dominion kW demands; whereas Bear Island's total annual delivered energy is approximately 5.5 percent of total annual Old Dominion energy.... If Old Dominion transfers one dollar of costs from energy to demand, then based on these 2004 loads, Bear Island would reduce its energy costs by 5.5 cents, but only increase its demand costs by 1.5 cents. [Thus], Bear Island would reduce its costs by 4.0 cents for every dollar of costs incurred by Old Dominion that is shifted from energy to demand.<sup>31</sup>

According to NOVEC, the other Members (for instance NOVEC) will bear the cost of the four cents to every dollar—a total of \$54,000 annually—saved by Bear Island as a result of the reclassification of Account 553.<sup>32</sup>

16. To support the classification of Account 553 as energy-related, NOVEC references the justification provided in Applicants' filing in Docket No. ER05-309-000 on December 7, 2004.<sup>33</sup> The filing states, *inter alia*, that Account 553 expenses "are variable in nature and largely depend on the number of required

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<sup>28</sup> NOVEC RB at 28 (citing 18 C.F.R. § 385.205 (2006)).

<sup>29</sup> *Id.* NOVEC suggests that it timely raised its protest to Applicants' reclassification of Account 553 to demand-related by raising the issue in its testimony. *See id.* at 26–27. According to NOVEC, Applicants decided to classify Account 553 as demand-related only as a result of the Settlement, and NOVEC's testimony was not due until after the occurrence of the Settlement. *Id.*

<sup>30</sup> NOVEC IB at 22.

<sup>31</sup> *Id.* at 22–23 (citing Ex. NVC-1 at 6:13–14, 18–22).

<sup>32</sup> *Id.* at 23 (citing Ex. NVC-1 at 15:19–20; Ex. ODC-10 at 85:10–16).

<sup>33</sup> *Id.* at 23–24.

starts and the amount of generation from facilities over time.”<sup>34</sup> The original filing also provides that the energy-related classification is “in keeping with PJM guidelines,”<sup>35</sup> and thus NOVEC concludes that classifying Account 553 as energy-related is consistent with PJM’s method.<sup>36</sup> NOVEC states that “[t]he Commission’s prior acceptance of this practice is sufficient evidence of the justness and reasonableness of the originally proposed classification.”<sup>37</sup> Finally, NOVEC argues that implementation of an energy-related classification will have no impact on the Settlement or the parties to the Settlement.<sup>38</sup>

17. NOVEC alleges that neither Staff nor Applicants have shown that the classification made in Applicants’ original filing is not just and reasonable, and the fact that the Commission approved a different classification with respect to the Settlement does not alone make an energy-related classification unjust or unreasonable.<sup>39</sup> NOVEC Witness Arsuaga proposes certain modifications to the rate formulas filed in these proceedings in order to “carve-out” NOVEC from the impact of the demand-related classification of Account 553 in the Settlement. These proposals are contained in Exhibits NVC-2 (corrected) and NVC-3 (corrected). NOVEC argues that, if the Commission accepted the position that Applicants’ original filing governs with respect to Account 553, Applicants Witness J. Bertram Solomon (Applicants Witness Solomon) has acknowledged that Account 553 would be classified as energy-related and that Mr. Arsuaga’s proposed adjustment to reclassify Account 553 from demand- to energy-related would be appropriate.<sup>40</sup>

### Staff

18. Staff asserts that Applicants bear the burden to show that their proposed allocation of Account 553 is just and reasonable.<sup>41</sup> Staff maintains, however, that Applicants need not disprove the reasonableness of alternative allocations.<sup>42</sup>

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<sup>34</sup> Application for Acceptance of Initial Tariff, Notice of Cancellation of Existing Tariff and Request for Waivers, Docket No. ER05-309-000 (December 7, 2004).

<sup>35</sup> *Id.*

<sup>36</sup> NOVEC RB at 4.

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

<sup>39</sup> NOVEC IB at 24.

<sup>40</sup> *Id.* at 22 (citing Tr. at 300:22–25, 301:1, 301:16–20).

<sup>41</sup> Staff RB at 18.

<sup>42</sup> *Id.*

19. Staff believes it has shown that allocating Account 553 based on demand is just and reasonable<sup>43</sup> and that NOVEC has not shown to the contrary.<sup>44</sup> Moreover, Staff argues that allocating Account 553 to energy is unjust and unreasonable.<sup>45</sup> To explain the nature of energy-related charges and why Account 553 differs, Staff cites to Applicants' response to data request Staff-ODEC-57, which explains that "[e]nergy-related charges are *variable* charges that can be tied directly to power production and consumption, increasing as production increases to meet consumption needs, and decreasing as consumption decreases."<sup>46</sup> Applicants state that the essence of Account 553 is maintenance, and although "[i]ncreased production will increase the need for maintenance...maintenance is not generally regarded as *directly* related to production and consumption in a given period."<sup>47</sup> Rather, "[m]aintenance is performed to keep a unit fit for service, *i.e.*, available when called upon, as well as available for future use."<sup>48</sup> Thus, Staff Witness Allison L. Browning (Staff Witness Browning) concludes that Account 553 is "more of a demand-related charge [than energy-related] because the units need to be there to run."<sup>49</sup> Ms. Browning also testifies that the fact that a classification based on demand may result in higher charges for NOVEC does not alone make the classification unreasonable.<sup>50</sup>

## Applicants

20. Although the initial filings in these dockets classified Account 553 as energy-related, Applicants note that they corrected the classification of Account 553 by returning it to a demand-related account in their Witness Solomon's direct testimony.<sup>51</sup> Applicants

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<sup>43</sup> *Id.*

<sup>44</sup> *Id.* Staff also argues that the application filed in Docket No. ER05-309-002 on December 7, 2004, which NOVEC cites to support its position, is not part of the record in this proceeding. *Id.* at 17.

<sup>45</sup> *Id.* at 20.

<sup>46</sup> Staff IB at 21 (quoting Ex. S-3 at 2) (emphasis added).

<sup>47</sup> *Id.* (quoting Ex. S-3 at 2).

<sup>48</sup> *Id.* (quoting Ex. S-3 at 2).

<sup>49</sup> *Id.* at 21–22 (quoting Tr. at 443:11–13); Staff notes Applicants Witness Solomon similarly testifies that the expenses booked to Account 553 are for maintenance and that they "are predominantly fixed in nature rather than varying more directly with energy output." *Id.* at 21 (quoting Ex. ODC-8 at 16:18–17:2).

<sup>50</sup> Staff RB at 18 (citing Ex. S-1 at 7:7–10).

<sup>51</sup> Applicants IB at 33–35 (citing Ex. ODC-6 at 7:18–21; Ex. ODC-8 at 13:5–14:3, 15:5–19:8). Applicants allege that Mr. Solomon agrees with Mr. Arsuaga's "carve-out"

point out that Mr. Solomon's direct testimony was filed well before the Settlement, and thus the choice to classify the account as demand-related was not made by virtue of the Settlement, but rather without reference to the Settlement.<sup>52</sup> Applicants conclude that Account 553 is properly classified as demand-related<sup>53</sup> and there is no need to "carve-out" NOVEC from the Settlement with respect to Account 553.<sup>54</sup>

21. Indeed, Applicants assert that NOVEC has provided no evidence to show that the demand-related classification is unjust and unreasonable.<sup>55</sup> According to Applicants, NOVEC's view that "reclassifying" Account 553 as demand-related will increase rates fails to consider that Account 553 has traditionally been demand-related.<sup>56</sup> Moreover, Applicants argue that the change of the classification from energy-related to demand-related would cause a rate increase only in isolation from the elements of the Settlement benefiting the Members.<sup>57</sup> Applicants agree with Staff that a rate increase does not alone render the classification of Account 553 unjust and unreasonable.<sup>58</sup> Finally, Applicants allege that NOVEC Witness Arsuaga's assumptions, in determining that a demand-related classification will cause a rate increase, are "unreasonably unrealistic, producing exaggerated results that were of little value."<sup>59</sup>

22. Similarly, Applicants contend that NOVEC is not entitled to an adjustment designed to "reverse the reclassification of \$2,346,198 of expenses from demand to energy" in the year 2005.<sup>60</sup> Applicants explain that, although Section 1.04 of the Settlement references the reclassification, the reclassification merely reflects an adjustment that became necessary when the Commission denied Applicants' request for an earlier effective date for rate formulas proposed in Docket No. ER05-360-000.<sup>61</sup>

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of NOVEC from the Settlement with respect to Account 553 *only to the extent that* the Commission adopts the New Dominion Tariff as it was initially filed in these proceedings despite the contrary testimony of Applicants and Staff. Applicants RB at 10.

<sup>52</sup> Applicants IB at 35–36.

<sup>53</sup> *Id.* at 35.

<sup>54</sup> *Id.* at 35, 37.

<sup>55</sup> *Id.* at 37; Applicants RB at 11.

<sup>56</sup> Applicants RB at 10.

<sup>57</sup> *Id.*

<sup>58</sup> *Id.*

<sup>59</sup> *Id.* (comparing Ex. ODC-12 to Exs. NVC-3 (corrected), NVC-4 (corrected), and NVC-5 (corrected)).

<sup>60</sup> Applicants IB at 36 (quoting Ex. NVC-1 at 16:26–31).

<sup>61</sup> *Id.* at 36–37.

## B. Discussion and Ruling

23. NOVEC is wrong that Applicants were required to amend their initial filing in this proceeding classifying Account 553 as energy-related. Rule 205 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.205 (2006), cited by NOVEC, requires, *inter alia*, a utility company to make a rate filing with the Commission in order to change a classification contained in an *established* rate schedule. The energy-related classification of Account 553 was proposed in Applicants' section 205 filings, which the Commission accepted only subject to the instant hearing procedures.<sup>62</sup> The energy-related classification thus has not been established by the Commission but rather is only part of a proposed set of rates. Prior to Applicants' filings in this proceeding, the established classification of Account 553 was already demand-related, as Applicants now propose to keep it. While amending the rate filings may have been prudent, it would be empty formalism to refuse Staff and Applicants' request to classify Account 553 as demand-related solely on the basis that Applicants' initial filing contains an energy-related classification.<sup>63</sup>

24. The burden of proof is irrelevant here, as Staff and Applicants have shown that a demand-related classification is just and reasonable, and NOVEC has not rebutted that showing.<sup>64</sup> Applicants and Staff offer credible evidence supporting the justness and reasonableness of a demand-related classification. As noted in their briefs, both Staff Witness Browning and Applicants Witness Solomon testify that energy-related charges

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<sup>62</sup> See *New Dominion Energy Coop.*, 110 FERC ¶ 61,275 at P 27.

<sup>63</sup> In *City of Winnfield v. FERC*, 744 F.2d 871 (D.C. Cir. 1984) (*Winnfield*), where the Commission had rejected a utility's new rate design and instead upheld a Staff proposal to implement a rate increase while retaining the preexisting rate design, the court rejected a customer's argument that the Commission "must act within the confines of the utility's proposals." *Id.* at 875. The court found that the structure of the FPA is not threatened when in a section 205 proceeding the Commission rejects the utility's new rate design "but grants a rate increase under the form the utility had previously been using," which the utility accepts. *Id.* The Commission also found that customers had sufficient notice of the Staff proposal since it retained the preexisting scheme and was described in Staff's pre-filed testimony. *Id.* at 876. I find that the reasoning of *Winnfield* pertains here. Like the customer in *Winnfield*, NOVEC had sufficient notice of the proposal to keep Account 553 demand-related since Applicants stated their intent to return the classification of Account 553 to demand-related in their pre-filed testimony.

<sup>64</sup> If NOVEC bore the burden of proof, it would as an initial matter have to show that the proposed, demand-related, classification is unjust and unreasonable, which it has failed to do. If Applicants bore the burden of proof, they would have to show that the demand-related classification is just and reasonable, which they have done.

are variable in nature and that the maintenance-type expenses charged to Account 553 are more fixed in nature and thus more appropriately charged to demand. In fact, NOVEC essentially concedes that a demand-related classification is just and reasonable. In its initial brief, NOVEC states: “Although Applicants reclassified Account 553 to demand [under the Settlement], neither Applicants nor Staff have produced any evidence that [an energy-related] classification is not *also* just and reasonable.”<sup>65</sup> NOVEC’s argument that a switch in the classification of Account 553 from energy-related to demand-related would result in an increase to NOVEC’s rates misses the point. As Staff and Applicants note, the fact that a demand-related classification may result in a higher charge to NOVEC does not alone make the classification unreasonable.<sup>66</sup> NOVEC offers no additional evidence to show that the demand-related classification is unjust and unreasonable.

25. Applicants and Staff have shown that a demand-related classification is just and reasonable, and NOVEC has not shown to the contrary. Accordingly, I find that the proper classification of Account 553 is demand-related.

### **Issue 3: Is Applicants’ market-based rates proposal just and reasonable?**

26. The Commission granted New Dominion market-based rates authority in the March 8 Order.<sup>67</sup> Staff challenges the justness and reasonableness of the market-based rates provision contained in the New Dominion Tariff and requests that Applicants add certain language to the tariff to protect against discriminatory treatment among the Members. Applicants agree, in part, to Staff’s request. Because Staff has failed to justify the need for additional language in the New Dominion Tariff, I will not require Applicants to add language to the tariff other than that to which they have agreed.

#### **A. Positions of the Parties**

##### **Staff**

27. Staff contends that Applicants’ proposed market-based rates are not just and reasonable because the New Dominion Tariff does not specify how market-based rates

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<sup>65</sup> NOVEC IB at 24 (emphasis added).

<sup>66</sup> The standard of section 205 of the FPA is whether the proposed rate changes are just and reasonable. 16 U.S.C. § 824d (2000). Utilities must be able to make changes in their rate formulas to reflect current circumstances. The fact that a change may increase charges to customers does not alone make a proposed rate formula, or an element thereof, unjust and unreasonable.

<sup>67</sup> *New Dominion Energy Coop.*, 110 FERC ¶ 61,275 at P 30–41, p. 18.

would be applied to customers of New Dominion, including its Member Cooperatives.<sup>68</sup> Staff Witness Browning testifies that

[t]here are no criteria in the tariff by which New Dominion will decide who will be charged which rate. Because New Dominion would be wholly-owned by the Member Cooperatives, such an implementation of the market-based and cost-based tariffs proposed by New Dominion could result in discriminatory cost shifts among similarly situated Member Cooperatives. Moreover, the market-based and cost-based tariffs proposed by New Dominion would allow New Dominion to engage in such cost shifts at will and thereby would enable discriminatory pricing.<sup>69</sup>

Staff argues that although Applicants' market-based rate proposal provides criteria by which New Dominion *may offer* market-based rates to Member Cooperatives' new and expanding loads, Applicants' market-based rate proposal does not provide *any* criteria under which a Member Cooperative *would receive* market-based rates.<sup>70</sup> Accordingly New Dominion could offer market-based rates to some Member Cooperatives and deny market-based rates to other similarly situated Member Cooperatives.<sup>71</sup> Staff Witness Browning recommends that Applicants could cure this problem by adding the language contained in Section 1.01 of the Settlement.<sup>72</sup> Staff Witness Browning also recommends that the Applicants be required to fulfill all Member Cooperatives' market-based rate

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<sup>68</sup> Staff IB at 22; Staff RB at 12.

<sup>69</sup> Ex. S-1 at 8:10–19.

<sup>70</sup> Staff IB at 24.

<sup>71</sup> *Id.*

<sup>72</sup> Ex.S-1 at 9:8–19. Section 1.01 states in pertinent part:

[W]ith the exception of sales made upon request of a Member Cooperative and pursuant to the Board Resolution and the Board of Directors Policy Manual Market Based Rates for New or Expanding Loads attached hereto, which provides for sales at market-based rates for Member Cooperative load related to new customers, or expansion of existing customers, in excess of 1,000 kW...New Dominion's Member Cooperatives will not be subject to market-based rates, including any rates contemplated by 'Attachment E: FERC Electric Tariff Original Volume No. 2 Market-Based Rates' filed on October 5, 2004, and amended on January 7, 2005.

*Id.*

requests that meet the Applicants' voluntary criteria with regard to new and expanding loads.<sup>73</sup>

## Applicants

28. Applicants maintain that, since Old Dominion first received authorization to charge market-based rates in 1997, it has never been accused of abusing its authority.<sup>74</sup> Applicants also note that the Commission has granted New Dominion unconditional market-based rates authority.<sup>75</sup> Applicants nonetheless agree to include a provision in the New Dominion Tariff which reflects its Board Policy that all sales to the Members will be made at cost-based rates, with the exception of specific types of sales to new and expanding load.<sup>76</sup>

29. Applicants see no need, however, for the additional language proposed by Staff stating that Applicants must fulfill the market-based rate requests of all Members that qualify under Applicants' market-based rates policy (the Policy).<sup>77</sup> Applicants argue that the Policy, formally adopted by the Old Dominion Board, makes clear that Applicants will not offer market-based rates discriminatorily.<sup>78</sup> The Policy provides that "Old Dominion will provide a wholesale rate for its Members that will give them the option of offering market-based pricing under limited term contracts, not to exceed five years, to

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<sup>73</sup> *Id.* at 10:6–12.

<sup>74</sup> Applicants IB at 39; Applicants RB at 41.

<sup>75</sup> Applicants RB at 41.

<sup>76</sup> Applicants IB at 39 (citing Ex. ODC-14 at 4:9–8:2). The precise language Applicants agree to include reads as follows:

With the exception of sales made upon request of a Cooperative pursuant to the Board of Directors Policy Manual, "Market-Based Rates for New or Expanding Loads," which provides for sales at market-based rates for Cooperative Load related to new customers, or expansion of existing customers, in excess of 1,000 kW, all sales to Cooperatives will be made pursuant to this tariff. Except as specifically provided above, the Cooperatives will not be subject to market-based rates, including any rates contemplated by FERC Electric Tariff Original Volume No. 2 Market-Based Rates filed on October 5, 2004, and amended on January 7, 2005.

Ex. ODC-15.

<sup>77</sup> Applicants RB at 41.

<sup>78</sup> *Id.* at 42.

all loads meeting [certain] criteria.”<sup>79</sup> According to Applicants, “[t]hat statement clearly asserts that the [market-based rates] pricing *will* be made available so that the Members *will* have the option to offer it to *all* load meeting the criteria.”<sup>80</sup> Thus, Applicants conclude, the Policy does not allow them the discretion to offer market-based rates to some Members and not others.<sup>81</sup> Additionally, Applicants maintain that the language they have agreed to add to the New Dominion Tariff in this proceeding, *see supra* note 76, will make it “abundantly clear” that a Member may choose to offer a market-based rate to a customer meeting the criteria outlined in the Policy, but Members will not be subject to market-based rates against their will.<sup>82</sup>

30. In sum, Applicants believe their proposed approach is just and reasonable and that further limitations are unnecessary.<sup>83</sup> Accordingly, Applicants request that the undersigned Presiding Judge recognize the conditions Applicants have agreed to accept but reject Staff’s request for additional limitations.<sup>84</sup>

## B. Discussion and Ruling

31. In the March 8 Order, in Docket Nos. ER05-20-000 and ER05-20-001, the Commission found that New Dominion’s application for market-based rates satisfied Commission standards and accordingly granted Applicants market-based rates authority, without setting the matter for hearing.<sup>85</sup> Although the Commission found no problem with Applicants’ proposed market-based rates, Staff insists Applicants must add additional language to the New Dominion Tariff to protect against discriminatory treatment among the Members. Staff fails to proffer any authority requiring the type of language it proposes. Applicants nonetheless agree to add language to the New Dominion Tariff stating essentially that, with the exception of sales made at the request of a Member and under the Board of Directors Policy Manual, all sales to Members will

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<sup>79</sup> Ex. ODC-3. The specified criteria are: (1) “A new customer load of 1000 kilowatts or more connected to a Member system of Old Dominion,” and (2) “[a]n expansion of a load at the facility of an existing customer of a Member system of Old Dominion that increases the load by 1000 kilowatts or more.” *Id.*

<sup>80</sup> Applicants RB at 43.

<sup>81</sup> *Id.*

<sup>82</sup> *Id.* at 43–44.

<sup>83</sup> *Id.* at 44. Applicants opine that adding Staff’s additional proposed language adds nothing to the tariff not already covered by the terms of the FPA prohibiting discriminatory treatment. *Id.* at n.20.

<sup>84</sup> *Id.* at 44–45.

<sup>85</sup> March 8 Order at P 30–41, p. 18.

be made under the New Dominion Tariff and not at market-based rates. Staff concludes that the language Applicants agree to include in the New Dominion Tariff is consistent with the Staff-proposed language.<sup>86</sup> As Applicants note, the language of their stated market-based rates policy (*i.e.* the Policy) and the language Applicants have agreed to add to the New Dominion Tariff in this proceeding will protect against discriminatory treatment among the Members. Staff has failed to justify the need for any additional changes at this time.

#### **Issue 4: Is the depreciation methodology proposed by Applicants just and reasonable?**

32. The formula rate in the Old Dominion Tariff and the formula rate in the New Dominion Tariff include a depreciation expense.<sup>87</sup> Although Applicants have proposed no changes to the depreciation expense in this proceeding,<sup>88</sup> Staff challenges Applicants' past practice of changing their depreciation rates and methodology without Commission approval. Applicants state that they agree to follow Staff's suggested procedure for modifying their depreciation methodology and rates in the future. I find that Staff has not shown Applicants' depreciation methodology to be unjust and unreasonable and therefore conclude that no changes to Applicants' depreciation methodology are necessary at this time.

#### **A. Positions of the Parties**

##### **Staff**

33. Staff Witness Browning testifies that depreciation expense is a component of the rate or rate formula and that the Commission requires a company to make a formal request for approval of a proposed change in depreciation rates before implementing the proposed change.<sup>89</sup> Because Applicants could change their depreciation methodology at any time under their filing, Staff concludes the methodology is not just and reasonable.<sup>90</sup>

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<sup>86</sup> Staff IB at 36.

<sup>87</sup> Ex. ODC-5 at Original Sheet No. 3; Ex. ODC-4 at Original Sheet No. 11.

<sup>88</sup> See Ex. S-5.

<sup>89</sup> Staff IB at 25 (citing *Midwest Power Sys., Inc.*, 67 FERC ¶ 61,076 at 61, 209 (1994) (*Midwest Power*)); Staff RB at 13. Staff also asserts that section 302 of the FPA, 16 U.S.C. § 825a (2000), requires the same. Staff IB at 25–26; Staff RB at 13.

<sup>90</sup> Staff IB at 26. Staff also argues that because Applicants accept that changes to the depreciation methodology are appropriate, they essentially have conceded that the rate filings are not just and reasonable. Staff RB at 13–14.

Accordingly, Staff requests that the undersigned Presiding Judge find that “[t]he depreciation methodology proposed by Applicants is not just and reasonable.”<sup>91</sup>

### Applicants

34. Applicants agree “to adopt Staff witness Browning’s position that a formal request for FERC approval must be made when seeking to change...depreciation rates in the future.”<sup>92</sup> Applicants allege, however, that when a revised depreciation rate is filed with the Commission it may be implemented at the end of the suspension period, subject to refund, or, subject to refund, pending settlement judge procedures and “possibly a full hearing on the matter.”<sup>93</sup> According to Applicants, “[n]o further action on this issue is contemplated at this time.”<sup>94</sup>

### B. Discussion and Ruling

35. As Staff correctly notes, section 302 of the FPA,<sup>95</sup> as the Commission applied it in *Midwest Power*, mandates a utility company to submit a formal request to the Commission asking for approval of a proposed change in its depreciation rate before implementing the change.<sup>96</sup> Because Applicants acquiesce to Staff’s request that they apply to the Commission for future changes in their depreciation rates, there is no dispute on this matter.<sup>97</sup> It is not clear what further action Staff contemplates, but I find that no

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<sup>91</sup> Staff IB at 40.

<sup>92</sup> Applicants IB at 40; *see also* Applicants RB at 45.

<sup>93</sup> Applicants RB at 45–46 (citing *Wisconsin Pub. Serv. Corp.*, 110 FERC ¶ 61,192 (2005) (*Wisconsin Public Service*); *Virginia Elec. & Power Co.*, 53 FERC ¶ 61,047 (1990); *Virginia Elec. & Power Co.*, 19 FERC ¶ 61,195 (1982)).

<sup>94</sup> Applicants IB at 40; *see also* Applicants RB at 46.

<sup>95</sup> 16 U.S.C. § 825a (2000).

<sup>96</sup> *Midwest Power*, 67 FERC ¶ 61,076 at 61,209.

<sup>97</sup> In their Reply Brief, Applicants raise the matter of *when* a revised depreciation rate pending approval from the Commission may take effect. Because Applicants failed to raise this issue until the filing of their Reply Brief, it is not properly before me. Regardless, it is unclear what action Applicants request as to this issue. I do note, however, that in *Midwest Power*, the Commission stated that a formal request for approval of revised depreciation rates may be made “as part of a filing of proposed revised electric rates,” or “[a]s an alternative, a utility could file a request for a declaratory order asking for approval of its proposed revised depreciation rates.” *Midwest Power*, 67 FERC ¶ 61,076 at 61,209. The Commission’s hearing order in *Wisconsin Public Service*, cited by Applicants, makes clear that when a utility files for a

changes to the rate formulas with respect to Applicants' depreciation methodology are necessary at this time.

**Issue 5: Are the reactive power charges proposed by Applicants just and reasonable?**

36. Applicants propose to keep the reactive power rate, set at \$0.06/rkVA, unchanged from their previously-approved rate formulas, although they agree to modify the rate as part of a future section 205 filing. Staff argues that the reactive power rate is unjust and unreasonable and must be changed as part of the instant proceeding. Because Staff has not shown that the current reactive power rate is unjust and unreasonable, I will not require Applicants to revise the rate at this time.

**A. Positions of the Parties**

**Staff**

37. As an initial matter, it is Staff's position that Applicants bear the burden of proof to justify their filed reactive power charge. Staff contends that, because the Applicants' rate filings in this case were made under section 205 of the FPA,<sup>98</sup> Applicants bear the burden of proof on all issues including the reactive power charge.<sup>99</sup> According to Staff, the United States Court of Appeals for the District of Columbia (D.C. Circuit) has held that "the party filing a rate adjustment with the Commission under [section 205] bears the burden of proving the adjustment is lawful."<sup>100</sup> Staff also notes that in the March 8 Order

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change in its depreciation rates, the Commission may, after suspending the revised depreciation rates for a nominal period, accept them for filing subject to refund pending settlement judge and hearing procedures. *Wisconsin Public Service*, 110 FERC ¶ 61,192 at P 8.

<sup>98</sup> 16 U.S.C. § 824d (2000).

<sup>99</sup> Staff IB at 13–15; Staff RB at 41 (citing 16 U.S.C. § 824d (e) (2000) for the notion that Applicants bear the burden of proof with respect to rate increases). Staff cites *FPC v. Tennessee Gas Transmission Co.*, 371 U.S. 145, 152 (1962) and *Laclede Gas Co. v. FERC*, 670 F.2d 38, 41 (Former 5th Cir. 1982) (*Laclede*) for the proposition that a utility filing for a rate increase assumes the risk and bears the burden of establishing a proposed rate schedule as just and reasonable. Staff RB at 41. Staff makes the additional points that the burden of proof is a threshold issue and that proposed changes to a rate formula are tantamount to changes to the filed rate and cites numerous cases and regulations as authority for those points. *See id.* at 14 and n.24–27.

<sup>100</sup> Staff RB at 5 (citing *Alabama Power Co. v. FERC*, 993 F.2d 1557, 1570 (D.C.

the Commission set for hearing the justness and reasonableness of Applicants' wholesale rates.<sup>101</sup> Staff continues that the Commission has held that, when it sets for hearing the justness and reasonableness of a matter, the hearing may include all issues relevant to an assessment of the justness and reasonableness and is not limited to issues explicitly identified.<sup>102</sup> Staff suggests that since the scope of this proceeding includes whether the formula rates filed by Applicants are just and reasonable,<sup>103</sup> "Applicants have an affirmative duty to support the entirety of their filings, including *all* of the proposed formula rates."<sup>104</sup>

38. Staff recognizes that Applicants do not propose to change the reactive power charge component of their formula rates. Staff maintains that Applicants nonetheless bear the burden of proof on this issue. Staff argues that Applicants' reliance on *Southern Co. Services*, 48 FERC ¶ 63,007 (1989) (*Southern*), is misplaced. Applicants contend that *Southern*, is inapposite because, unlike the instant case, it did not involve a full evidentiary hearing under section 205.<sup>105</sup> Rather, the Commission in *Southern* merely held that Staff bears the burden of proof under section 206 of the FPA,<sup>106</sup> which is not applicable here.<sup>107</sup>

39. While Staff concedes that the cases cited by Applicants hold that the filing party does not bear the burden of proof with respect to "constant elements,"<sup>108</sup> Staff alleges that more recent United States Courts of Appeals opinions hold that "where existing and proposed rate components interact to produce unjust and unreasonable results..., the filing party must forgo its presumption that the existing components will remain unchanged."<sup>109</sup>

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Cir. 1993) (*Alabama Power*)).

<sup>101</sup> Staff IB at 14–15.

<sup>102</sup> *Id.* at 15 (citing *Cincinnati Gas & Elec. Co.*, 59 FERC ¶ 61,072 at 61,291 (1992)).

<sup>103</sup> See Staff IB at 15–16 (citing Tr. at 77:10–13).

<sup>104</sup> *Id.* at 16 (emphasis added).

<sup>105</sup> Staff RB at 39.

<sup>106</sup> 16 U.S.C. § 824e (2000).

<sup>107</sup> Staff RB at 37–38. Staff also asserts that *Southern* stands for the proposition that, if Staff bore the burden of proof, it should have opened and closed the case, which did not occur in this case. *Id.* at 38–39.

<sup>108</sup> *Id.* at 39–40 (citing *Winnfield*, 744 F.2d at 877).

<sup>109</sup> *Id.* at 40 (citing *East Tenn. Natural Gas Co. v. FERC*, 863 F.2d 932, 942 (D.C. Cir. 1988) (*East Tennessee*); *North Penn Gas Co. v. FERC*, 707 F.2d 763, 769 (3d Cir. 1983) (*North Penn*); *City of Batavia v. FERC*, 672 F.2d 64, 76–77 (D.C. Cir. 1982)

Staff also asserts that the Commission distinguishes between cases involving rate methodology features such as allocation and rate design, and those involving changes in rates such as cost of service.<sup>110</sup> As to the latter, Staff argues that “where the unchanged rate element is a component of the overall cost of service, the filing party bears the burden of proof as to the entire cost of service...because the unchanged components of the cost of service are an integral part of the overall cost of service.”<sup>111</sup> Applying that rule here, Staff argues that the reactive power charge is a component of New Dominion’s cost of service formula and thus Applicants bear the burden of proof.<sup>112</sup> Staff also suggests that, since, unlike the cases cited by Applicants, the instant case involves “a significant rate change pursuant to a corporate reorganization, a change to a formula rate, an integrated cost of service, and a likely rate increase,”<sup>113</sup> Applicants bear the burden of proof on all issues.<sup>114</sup>

40. Staff argues that Applicants have not satisfied their burden of proof, and moreover, even if Staff bears the burden of proof, Staff has proven the reactive power rate (rkVA) is unjust and unreasonable on three grounds.<sup>115</sup> First, Staff alleges that Applicants fail to adequately support the proposed rate. Staff Witness Edward A. Gross (Staff Witness Gross) testifies that “[a]part from the brief descriptions of the determination of reactive power demand, the rkVA rate, and the Reactive Power Charge, the Applicants’ filing does not provide any information regarding reactive power [or] explain how Applicants determined the filed rkVA rate.”<sup>116</sup> Staff also claims that Applicants Witness Solomon “admits that Applicants cannot support...the development of the proposed reactive power rate.”<sup>117</sup>

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(*Batavia*); *Laclede*, 670 F.2d at 42; *Northern Border Pipeline Co.*, 89 FERC ¶ 61,185 at 61,576 (1999) (*Northern Border*)).

<sup>110</sup> *Id.* (citing *Northern Border*, 89 FERC ¶ 61,185 at 61,575).

<sup>111</sup> *Id.* (citing *North Penn*, 707 F.2d at 769; *Northern Border*, 89 FERC ¶ 61,185 at 61,576).

<sup>112</sup> *Id.* at 42.

<sup>113</sup> *Id.* at 41. Specifically, Staff asserts that the inclusion of federal and state income taxes in the proposed rate formula for New Dominion and the proposal to allow New Dominion to make market-based sales represent a significant rate change and possible rate increase. *Id.*

<sup>114</sup> *Id.*

<sup>115</sup> *Id.* at 42–43.

<sup>116</sup> *Id.* at 42 (quoting Ex. S-6 at 6:17–22).

<sup>117</sup> *Id.* at 43 (citing Tr. at 327:15–19).

41. Second, Staff argues that Applicants' reactive power charges fail to reflect cost causation.<sup>118</sup> Staff supports its argument by describing Applicants' method of implementing the reactive power rate for billing purposes. Staff quotes Applicants Witness Solomon's testimony that "[t]he revenues from application of the reactive demand charge are credited against the demand costs in calculating the resulting demand charge,"<sup>119</sup> which is applied to each Member's billing demand in order to allocate the demand costs.<sup>120</sup> According to Staff, Mr. Solomon admits that the current reactive power charges fail to collect all of Applicants' reactive power costs, and the deficit is collected on the basis of coincident peak demands.<sup>121</sup> Staff states that the reactive power charges thus, instead of properly allocating reactive power costs on the basis of reactive demand, allocate them based on a hybrid of demand and reactive demand.<sup>122</sup> This allocation scheme, according to Staff, is likely to shift costs arbitrarily among the Members.<sup>123</sup> Staff cites *Sea Robin Pipeline Co v. FERC*, 795 F.2d 182, 188 (D.C. Cir. 1986) (*Sea Robin*), for the proposition that, in order for Staff to meet its burden to show that an unchanged rate is unjust and unreasonable, it is sufficient to show that the unchanged rate does not fully recover the costs of service to the customer.<sup>124</sup>

42. Third, Staff avers that the reactive power rate "has no connection to the reactive power costs paid by Applicants."<sup>125</sup> Staff maintains that the \$0.06/rkVA rate is a historical rate no longer applicable to Applicants' reactive power activities.<sup>126</sup>

43. Additionally, Staff believes that it is not necessary that the reactive power costs were foreseeable or known at the time of the filing for the Commission to order Applicants to make changes to their reactive power rate.<sup>127</sup> Staff reasons that the undersigned Presiding Judge stated at the hearing in this proceeding that Applicants must support their rate filings based on "current circumstances, [which happen to include]

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<sup>118</sup> Staff IB at 29.

<sup>119</sup> *Id.* (quoting Tr. at 320:22–25).

<sup>120</sup> *Id.* at 30 (citing Tr. at 323:2–5).

<sup>121</sup> *Id.* (citing Tr. at 323:6–20; Ex. ODC-8 at 46:18–23); Staff RB at 44.

<sup>122</sup> Staff IB at 30; Staff RB at 44.

<sup>123</sup> Staff IB at 30; Staff RB at 44. Staff explains that cost shifts would result from the fact that the distribution of reactive demand among the Members differs from the allocation of demand. Staff IB at 30–31.

<sup>124</sup> Staff RB at 43.

<sup>125</sup> Staff IB at 31.

<sup>126</sup> *Id.* at 31; Staff RB at 45–46.

<sup>127</sup> Staff RB at 48.

membership in PJM.”<sup>128</sup> According to Staff, Applicants could reasonably have foreseen, not only that they would join PJM, but also the timing and amount of reactive power purchases they would make from PJM.<sup>129</sup> In support, Staff asserts that, at the time of their rate filing in this proceeding, Applicants knew Old Dominion and New Dominion would be part of PJM and had reflected this fact in the New Dominion Tariff and in New Dominion’s cost of service formula.<sup>130</sup> Applicants Witness Solomon stated that, also at the time of filing, Applicants had examined Schedule 2 of the PJM Tariff and estimated the amount of the reactive power charges that would apply to Applicants.<sup>131</sup> Staff further notes that in May 2005 Applicants began conducting reactive power activities through PJM.<sup>132</sup> Staff avers that Applicants Witness Solomon acknowledged that “Applicants could have stated in their rate filing that reactive power charges paid to PJM would be allocated to [Members] on the basis of reactive power demand.”<sup>133</sup>

44. Staff also argues that the fact that Applicants’ proposed reactive power rate was incorporated into the Settlement has no bearing on the instant proceeding.<sup>134</sup>

45. Finally, consistent with the testimony of Staff Witness Gross, Staff recommends that, in lieu of the proposed \$0.06/rkVA reactive power rate, Applicants allocate their reactive power costs to the Members based on each Member’s reactive power demand.<sup>135</sup> Staff further states that Applicants should not delay the changes until a future section 205

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<sup>128</sup> *Id.* at 48–49 (quoting Tr. at 458:13–20).

<sup>129</sup> *See* Staff IB at 28.

<sup>130</sup> *Id.*

<sup>131</sup> *Id.* at 29 (citing Tr. at 333:25–334:8).

<sup>132</sup> *Id.* at 28 (citing Ex. S-6 at 7:8–10).

<sup>133</sup> *Id.* at 29 (citing Tr. at 375:24–376:10); Staff RB at 49 (citing Tr. at 334:18–335:15, 362:20–363:9, 375:22–376:10).

<sup>134</sup> Staff RB at 44–45.

<sup>135</sup> Staff RB at 47. *See also* Staff IB at 32, 38. In its Reply Brief, Staff describes at length its belief that Mr. Gross’ written testimony and live testimony on the proper method to allocate reactive power costs are consistent. Staff RB at 49–52. In short, Mr. Gross testifies that, since metered reactive power demand for each Member is known, it would be “a trivial exercise” to allocate reactive power charges to the Members on the basis of a proportionate share of the total costs paid to PJM. *Id.* at 50 (quoting Tr. at 453:25–454:6). Additionally, while Mr. Gross states his opinion on how Applicants should allocate the reactive power costs among the Members, Staff maintains that how Applicants choose to pass through the cost allocations “is a matter of rate design or rate structure.” *Id.* at 51–52.

filing.<sup>136</sup> Staff quotes *North Penn* as follows: “If a given methodology will result in unjust and unreasonable rates, the Commission may not permit its use. That conclusion holds true even if the company had employed that formulation in the past.”<sup>137</sup> Staff argues that the harm resulting from the application of unjust and unreasonable rates would far outweigh any administrative burden to the Applicants.<sup>138</sup>

## Applicants

46. Applicants argue that, with respect to provisions of the rate formula they do not seek to change, specifically the reactive power charge, the burden of proof falls not upon them, but rather upon the party seeking the change.<sup>139</sup> Specifically, Applicants assert that *Southern* stands for the proposition that Staff, as the proponent of change, must show that the filed reactive power rate is unjust and unreasonable and that Staff’s alternative is just and reasonable.<sup>140</sup> Applicants acknowledge that their filings provide no explanation of, or evidence in support of, their proposed reactive power rate.<sup>141</sup> They believe no such explanation is required since their proposed reactive power rate is unchanged from the prior rate formulas.<sup>142</sup> Applicants assert that Staff makes no specific proposal for the appropriate reactive power charges or how to determine them.<sup>143</sup> Thus, while Applicants agree that they *could* revise the rate formulas to reflect current allocations of reactive power charges<sup>144</sup> and even agree to make that change ultimately,<sup>145</sup> they argue that Staff has failed to satisfy the requisite burden of proof.<sup>146</sup> Applicants therefore argue that no changes should be required in this proceeding.<sup>147</sup>

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<sup>136</sup> Staff RB at 47.

<sup>137</sup> *Id.* at 47–48 (quoting *North Penn*, 707 F.2d at 767).

<sup>138</sup> *Id.* at 48.

<sup>139</sup> Applicants RB at 5–6, 53. *See also* Applicants IB at 44–45.

<sup>140</sup> Applicants RB at 5–6, 53. *See also* Applicants IB at 44–45. In *Southern*, the Commission relied on *Sea Robin; ANR Pipeline Co. v. FERC*, 771 F.2d 507 (D.C. Cir. 1985) (*ANR*); *Winnfield*; and *Public Service Commission of New York v. FERC*, 642 F.2d 1335 (D.C. Cir. 1980) (*Transco*). *See Southern*, 48 FERC ¶ 63,007 at 65,013.

<sup>141</sup> Applicants RB at 46–47.

<sup>142</sup> *Id.* at 48.

<sup>143</sup> Applicants IB at 44; Applicants RB at 53.

<sup>144</sup> Applicants IB at 45.

<sup>145</sup> *Id.* at 41.

<sup>146</sup> *Id.* at 44–45.

<sup>147</sup> *Id.* at 42.

47. In lieu of revising the reactive power rate in a compliance filing to this proceeding, Applicants propose filing the suggested changes in their next section 205 filing.<sup>148</sup> Applicants assert that delaying the change is appropriate because: (1) it would be an administrative burden to apply one method of setting reactive power charges to NOVEC and a different method to the other Members under the Settlement;<sup>149</sup> (2) current reactive power costs were not known or foreseeable at the time of the filings in this proceeding, and thus it would be “unfair and contrary to Commission practice” to require changes now;<sup>150</sup> (3) even if the \$0.06/rkVA charge fails to collect all the reactive power costs, the deficit will nonetheless be recovered through the demand charge, and thus the current method satisfies cost causation principles;<sup>151</sup> and (4) the amount of Old Dominion’s expected revenues for its reactive power contributions to PJM, which will be credited against the reactive power charges to the Members, is not determined yet.<sup>152</sup>

## B. Discussion and Ruling

48. I find that Staff bears the burden of proof to show that Applicants’ proposed reactive power charges are unjust and unreasonable and that Staff’s

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<sup>148</sup> *Id.* at 42, 44.

<sup>149</sup> *Id.* at 42; Applicants RB at 52–53.

<sup>150</sup> Applicants IB at 42–43. Specifically, Applicants state that, at the time they were preparing the filings in this proceeding, they had no experience with PJM reactive power charges and could not have known when Virginia Electric and Power Company’s (VEPCO) membership in PJM would be final. *Id.* at 42–43; Applicants RB at 48–50 (citing Ex. ODC-8 at 46:3–12). Applicants further clarify that “it was the *cost* of the Applicants’ reactive power purchases and the *identity* of the ultimate providers of the generator-supplied reactive power within the Virginia Power Zone...that was not reasonably foreseeable.” Applicants RB at 49 (citing Tr. at 332:21–333:12). Applicants assert that any information they learned when they began conducting reactive power activities through PJM in May 2005 is irrelevant as to what was foreseeable in September 2004 when the filings in this case were being prepared. *Id.*

<sup>151</sup> Applicants IB at 43; Applicants RB at 51–52. Applicants explain that they incur generator-supplied reactive power costs based on monthly CP (kW) demands, rather than metered reactive (rkVA) demands. Applicants IB at 43; Applicants RB at 51 (citing Ex. ODC-8 at 46:17–20). Thus, Applicants allege that the current method for collecting reactive demand costs better matches the way they are incurred under the PJM Open Access Transmission Tariff than Staff Witness Gross’ proposed method. Applicants IB at 43; Applicants RB at 51.

<sup>152</sup> Applicants IB at 43–44. Applicants elaborate that they await final approval of a settlement in a separate docket, the terms of which will dictate the reactive power revenue requirements for certain facilities. *Id.*

proposed replacement is just and reasonable. I find that Staff has not satisfied its burden of proof, and thus no action on the part of Applicants with respect to the reactive power charges is required at this time.

49. Applicants correctly state the general rule that under section 205 of the FPA a public utility does not bear the burden of proof as to unchanged components of a rate filing previously approved by the Commission. Rather, the proponent of the change has the burden of proof to demonstrate that the unchanged element is unlawful and the proposed rate change is lawful. The D.C. Circuit announced this rule in *Transco*, 642 F.2d at 1345, where a utility filed for a higher rate of return and at the ensuing hearing Staff proposed a new cost allocation methodology for the utility. The court held that, in order to preserve the structure and policy objectives of sections 4 and 5 of the Natural Gas Act (NGA) (and by analogy sections 205 and 206 of the FPA),<sup>153</sup> the Commission, when suggesting a change to a utility's rate methodology that the utility did not propose and does not support, must follow the procedures mandated by section 5 of the NGA and section 206 of the FPA, which place the burden of proof on the Commission as the proponent of change. The court thus found that Staff has the burden to show that an existing cost allocation methodology is unjust and unreasonable and that its proposed scheme is just and reasonable.<sup>154</sup>

50. Three later United States Courts of Appeals cases—*Batavia*, 672 F.2d at 76–77, *Laclede*, 670 F.2d at 42, and *North Penn*, 707 F.2d at 769—however, held that, at least in limited circumstances, FERC has authority under section 4 of the NGA and section 205 of the FPA to review an unchanged element of a proposed revised rate schedule and need not use the procedures of section 5 of the NGA and section 206 of the FPA. The court in *North Penn* stated that *Transco*'s holding, *i.e.* that the Commission must follow NGA section 5 (and by analogy FPA section 206) procedures when suggesting a change to a utility's rate

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<sup>153</sup> *Transco* concerned sections 4 and 5 of the NGA, 16 U.S.C. §§ 717c, d (2000), which are the NGA's equivalents of sections 205 and 206 of the FPA. Sections 4 and 5 of the NGA and sections 205 and 206 of the FPA have been treated by courts as identical in substance. *See, e.g., Winnfield*, 744 F.2d at 875. Thus, the discussion of the burden of proof issue, herein, discusses the case law in general terms as applicable to both statutes, whether the case concerned the NGA or the FPA.

<sup>154</sup> Five subsequent cases—*Winnfield*, 744 F.2d at 877, *ANR*, 771 F.2d at 513, *Sea Robin*, 795 F.2d at 186–87, *East Tennessee*, 863 F.2d at 942, and *Southern*, 48 FERC ¶ 63,007 at 65,013—followed *Transco*'s burden of proof holding and declared that the party proposing a change bears the burden of proof with respect to that change

methodology that the utility did not propose and does not support, is limited to cases where the change constitutes no part of, and is separate from, the rate increases sought in the filing.<sup>155</sup> When a proposed change is an “integral part” of the rate increase, on the other hand, NGA section 5 and FPA section 206 procedures are not required.<sup>156</sup>

51. Although the Commission, in *Southern*, 48 FERC ¶ 63,007 at 65,013, relied upon by Applicants, found that the *Transco* line of cases states the proper burden of proof rule, as Staff points out, a more recent Commission case, *Northern Border*, 89 FERC ¶ 61,185 at 61,575–76, makes clear that the Commission views the *North Penn* integral parts test as a limitation on the *Transco* rule.<sup>157</sup> In *Northern Border*, the utility filed a rate increase, which included no change to its pre-approved depreciation schedule. The Commission, however, raised an issue as to the depreciation schedule, and the utility argued it did not carry the burden of proof on that issue. The Commission disagreed. While the Commission did not overturn the *Transco* line of cases, it applied *North Penn*'s integral parts test as an exception to the *Transco* rule. According to the Commission, the utility bears the burden of proof not only as to changes it seeks to make to its rates but also as to any unchanging element of the rates that is an integral part of the proposed rate increase.<sup>158</sup> The Commission stated that *all* cost of service components including depreciation are integral parts of a proposed rate increase, and thus as to those issues the utility bears the burden of proof.<sup>159</sup>

52. Applying the rule as it was stated by the Commission in *Northern Border*, I find that Staff bears the burden of proof on the reactive power issue. The *Transco*

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<sup>155</sup> *North Penn*, 707 F.2d at 769.

<sup>156</sup> *See id.* at 769.

<sup>157</sup> The *Batavia* line of cases focused not on the burden of proof issue, but rather on the Commission's refund authority, *i.e.* whether it may order refunds pursuant to section 4 of the NGA and section 205 of the FPA, with respect to rate changes proposed by parties other than the filing utility. In *ANR*, 771 F.2d at 513–14, and *Sea Robin*, 795 F.2d at 187, the D.C. Circuit found that the *Batavia* rule was not applicable to the burden of proof issue. The court in *ANR*, for instance, found that *Batavia* and *Laclede* did not pertain because they involved only the issue of the Commission's suspension and refund authority and not the burden of proof issue. *ANR*, 771 F.2d at 513–14. The Commission in *Northern Border* differed from the reasoning of *ANR* and *Sea Robin* in this respect and found the *Batavia* line of cases applicable to the determination of who carries the burden of proof. *See Northern Border*, 89 FERC ¶ 61,185 at n.10.

<sup>158</sup> *See Northern Border*, 89 FERC ¶ 61,185 at 61,576.

<sup>159</sup> *Id.* at 61,574.

rule is implicated because Staff, not Applicants, is the proponent of change as to the reactive power rate. Moreover, the integral parts exception enunciated in *North Penn* does not apply in this case. The reactive power rate is not an integral part of the Applicants' rate proposals, which could result in an increase. Indeed, Staff maintains that Applicants' current reactive power charge may result in under-collection. Regardless, the reactive power charge is more a matter of cost allocation. Thus, as the proponent of change, Staff bears the burden of proof.

53. Staff fails to satisfy either prong of the requisite burden of proof. As to the first prong, Staff fails to show that the current rate is unjust and unreasonable. While Applicants concede Staff's point that the current reactive power charges may not fully collect Applicants' reactive power costs, Applicants explain that they incur generator-supplied reactive power costs based on monthly coincident peak demands, rather than metered reactive demands.<sup>160</sup> Staff offers no evidence to rebut this point, which serves to demonstrate that Applicants' current method for collecting reactive demand costs matches the way they are incurred under the PJM tariff. Additionally, Staff does not explain why it matters that Applicants' proposed reactive power rate represents a historical rate. Staff offers no evidence or authority to show that use of a historical rate is *per se* unjust and unreasonable.

54. With respect to the second prong of Staff's burden of proof, Staff fails to show that its alternative to Applicants' current reactive power charge is just and reasonable. In fact, Staff does not offer a fully developed alternative approach. While Staff argues that Applicants should allocate reactive power costs based on each Member's reactive power demand, Staff states that *how* Applicants choose to pass through the cost allocations "is a matter of rate design or rate structure."<sup>161</sup> Staff Witness Gross thus declines to propose an alternative methodology for Applicants' recovery of reactive power costs.

55. Because Staff has not satisfied its burden of proof, I find that no action is required of the Applicants at this time with respect to their reactive power rate. I note, however, that if Staff had shown that the current rate is unjust and unreasonable and had offered a just and reasonable alternative, Applicants would be required to change their reactive power rate in a compliance filing in this proceeding, regardless of the administrative burden.<sup>162</sup>

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<sup>160</sup> Cost causation principles are followed because, if the \$0.06/rkVA charge fails to collect all the reactive power costs, the deficit will be recovered through the demand charge.

<sup>161</sup> Staff RB at 51.

<sup>162</sup> In support of their argument that it would be unfair to require a change to the reactive power rate in this proceeding because the reactive power charges were not foreseeable at the time of filing, Applicants cite 18 C.F.R. § 35.13(a)(2)(i)(D) (2006).

**Issue 6: Is the allocation of cost responsibility among New Dominion's Members, as proposed by Applicants, just and reasonable?**

56. Staff and NOVEC raise an issue as to whether Applicants' current method of determining the demand rate by which demand charges paid by New Dominion will be passed through to the Members (Demand Rate) results in unjust and unreasonable allocations of demand charges to the Members. To develop the Demand Rate, Applicants apply the following formula (Demand Rate Formula):

$$\text{Demand Rate} = \frac{\text{Total Demand Expenses}}{\text{Total Delivery Point kW Demand} \\ \text{Less 300 kW minimum per Delivery Point}^{163}}$$

One component of the divisor is the sum of the demands of each Member. When there is no demand-side management agreement in place between Applicants and any of the Members or their customers, each Member's demand is measured by the Member's actual demand at the time of the combined monthly peaks of VEPCO and Old Dominion (Actual CP Demand).<sup>164</sup> As discussed *supra* P 5, the Settlement provides for Applicants and Bear Island, a customer of the Member Cooperative REC, to enter into a DSM Agreement. Section 3.2 of the DSM Agreement states that "[f]or purposes of calculating the monthly charge from REC to [Bear Island] for service to the Bear Island delivery point, Old Dominion/New Dominion will bill REC for 24,000 kW each month for the Term of this Agreement."<sup>165</sup> Thus, in determining the Demand Rate applicable to all Members, Applicants will use Actual CP Demand for all Members other than REC. But, with respect to the portion of REC's demand represented by service to Bear Island, the 24,000 kW stipulated by the DSM Agreement (DSM Agreement Demand) will be used in lieu of the Actual CP Demand. Both NOVEC and Staff take issue with the DSM Agreement's specification of Bear Island's load at 24,000 kW for purposes of calculating the Demand Rate. I find that use of the 24,000 kW figure to calculate the Demand Rate is reasonable and therefore reject NOVEC's and Staff's challenges relating to the DSM Agreement.

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This section, however, merely prescribes abbreviated filing procedures for utilities filing certain small rate increases. It does not address the matter here, *i.e.* what relief is appropriate if a utility's rate is found to be unjust and unreasonable.

<sup>163</sup> Ex. ODC-4 at Original Sheet No. 13.

<sup>164</sup> Ex. ODC-8 at 10.

<sup>165</sup> The Term of the Agreement is from November 1, 2005 until May 31, 2009. See Settlement, Attachment 2, at §§ 1.1, 3.1.

## A. Positions of the Parties

### NOVEC

57. NOVEC avers that the New Dominion Tariff at Section (E)(I)(a) mandates that the Demand Rate be based on each “Member Cooperative’s actual metered demand.”<sup>166</sup> NOVEC argues that Applicants’ current method of calculating the Demand Rate by using the DSM Agreement Demand for Bear Island, rather than Actual CP Demand, is unjust and unreasonable and unduly discriminatory.<sup>167</sup>

58. NOVEC explains that using the DSM Agreement Demand for Bear Island subjects NOVEC to higher rates.<sup>168</sup> NOVEC reasons that, all other things being equal, if the divisor in the Demand Rate Formula decreases, the Demand Rate will increase, resulting in higher demand charges to the Members (including NOVEC). Thus, according to NOVEC, if Bear Island’s Actual CP Demand exceeds the DSM Agreement Demand, use of the DSM Agreement Demand instead of Actual CP Demand will yield a higher Demand Rate and thus higher demand charges to the Members. NOVEC Witness Arsuaga testifies that, because Bear Island’s average demand is 68 MW and the DSM Agreement stipulates Bear Island’s demand as 24 MW, the DSM Agreement allows REC to reduce its total demand by 44 MW, which equates to a nearly \$6 million reduction in REC’s annual demand charges.<sup>169</sup> The costs avoided by REC, according to NOVEC, are shifted to the other Member Cooperatives and could increase NOVEC’s annual demand costs by nearly \$1.8 million.<sup>170</sup> NOVEC adds that it will bear the largest cost shift of all the Members due to its size.<sup>171</sup> NOVEC argues that shifting costs from REC to the other Member Cooperatives affords REC preferential treatment over the other Members, which

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<sup>166</sup> NOVEC IB at 14, 16 (“Applicants are...*required* to use *every member’s actual metered* demand during the hour in which the Old Dominion/VEPCO monthly coincident peak occurs”).

<sup>167</sup> *Id.* at 16.

<sup>168</sup> *Id.*

<sup>169</sup> *Id.* at 17. This conclusion is based on Mr. Arsuaga’s assumption that Applicants’ average imbedded demand cost is \$11.24/kW, which saves REC \$11,240/month for every MW of reduction in demand at the Bear Island delivery point. *See* Ex. NVC-1 at 12:13–16.

<sup>170</sup> NOVEC alleges that the cost shifts to NOVEC could reach nearly \$3 million. NOVEC IB at 17.

<sup>171</sup> *Id.* at 19.

are similarly situated, and thus violates section 205 of the FPA,<sup>172</sup> as well as principles of cost causation,<sup>173</sup> the filed rate doctrine,<sup>174</sup> and Commission policy.<sup>175</sup>

59. NOVEC disputes claims that it will benefit from the DSM Agreement.<sup>176</sup> NOVEC concedes that, if the DSM Agreement Demand exceeds Bear Island's Actual CP Demand, the use of the DSM Agreement Demand will benefit all the Member Cooperatives. NOVEC believes however that it is more likely that Bear Island's Actual CP Demand will be higher.<sup>177</sup> NOVEC maintains that, because the DSM Agreement gives Applicants only limited ability to curtail Bear Island's load, Applicants (and thereby NOVEC) bear the risk of loss under the DSM Agreement, not Bear Island.<sup>178</sup> NOVEC explains that, it is incumbent upon Applicants accurately to predict when system peak will occur, and, if they fail to do so, Bear Island may not curtail load to 24 MW, resulting in cost shifts to the other Members, as described above.<sup>179</sup>

60. Accordingly, NOVEC asks the Presiding Judge to find that Applicants may not use the DSM Agreement Demand, with respect to Bear Island, to determine the Demand Rate applicable to NOVEC. NOVEC argues that Bear Island's actual metered demand

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<sup>172</sup> *Id.* at 20 (citing 16 U.S.C. § 824e (b) (2006); *St. Michaels Utils. Comm'n v. FPC*, 377 F.2d 912, 915 (4th Cir. 1967); *Portland Gen. Exch., Inc.*, 51 FERC ¶ 61,108 at n.45 (1990)).

<sup>173</sup> NOVEC states that under the principle of cost causation the Commission, in developing rates, assigns costs to those that cause them. NOVEC RB at 20 (citing *Cities of Riverside & Colton v. FERC*, 765 F.2d 1434, 1439 (9th Cir. 1985); *Alabama Elec. Coop. Inc. v. FERC*, 684 F.2d 20 (D.C. Cir. 1982) (*Alabama Electric*); *Public Serv. Co. of N.H. v. New Hampshire Elec. Coop., Inc.*, 83 FERC ¶ 61,223 at n.33 (1998); *Indiana & Michigan Mun. Distrib. Ass'n v. Indiana Michigan Power Co.*, 59 FERC ¶ 61,260 at 61,956–57 (1992)). NOVEC argues it should not be responsible for costs it did not cause. NOVEC RB at 20 (citing *KN Energy Inc. v. FERC*, 968 F.2d 1295, 1300 (D.C. Cir. 1992) (*KN Energy*)).

<sup>174</sup> *Id.* at 21 (citing 18 C.F.R. § 35.1(e) (2006); *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 (1981) (*Hall*)).

<sup>175</sup> *Id.* at 20; NOVEC RB at 16–22. NOVEC states that past violations do not condone current practice. NOVEC RB at 17 (citing *City of Holland v. Midwest Indep. Sys. Operator*, 111 FERC ¶ 61,076 at P 22 (2005)).

<sup>176</sup> NOVEC RB at 12–16.

<sup>177</sup> NOVEC IB at 18.

<sup>178</sup> NOVEC RB at 9. NOVEC also alleges that the DSM Agreement is less favorable to Applicants than past such agreements. *Id.* at 15–16.

<sup>179</sup> *Id.* at 13–15.

for 2005 (2005 Demand) is not a proper measure either.<sup>180</sup> NOVEC explains that using 2005 figures would create a mismatch, such that rates for future years would be based on 2005 data rather than the data for the corresponding year of service.<sup>181</sup> Additionally, since there was no demand-side management agreement in place in 2005, NOVEC opines that Bear Island had greater incentive to curtail its load and thus may have behaved differently than it will in future years.<sup>182</sup> NOVEC's view is that it is inappropriate to try to estimate what Bear Island's demand might have been in future years absent the DSM Agreement. Rather, NOVEC concludes that Applicants must use Bear Island's Actual CP Demand in calculating the Demand Rate applicable to NOVEC.<sup>183</sup>

61. To ensure NOVEC's Demand Rate is calculated using Bear Island's Actual CP Demand, NOVEC argues that Applicants should implement a dual rate formula and apply it in a "cascading manner."<sup>184</sup> Specifically, NOVEC asserts that its costs should first be determined using Bear Island's Actual CP Demand. Then, Applicants should subtract NOVEC's costs from the Applicants' total costs and collect the remainder from the other eleven Members through application of the rate formulas adopted as part of the Settlement. Additionally, NOVEC argues that, because Applicants have been using the DSM Agreement Demand to determine rates for all Members, Applicants must correct the rates currently in effect as they apply to NOVEC by essentially carving NOVEC out from the impact of the DSM Agreement.<sup>185</sup>

### Staff

62. Staff argues that Applicants face potential over- or under-recovery of their demand costs as a result of the DSM Agreement and the fact that it requires a different demand determinant for Bear Island than would apply under the New Dominion Tariff.<sup>186</sup> Any potential benefit (*i.e.* over-recovery) of the DSM Agreement to the Members, Staff asserts is purely speculative. Staff states that any benefit is contingent upon Applicants' ability to manage curtailment of Bear Island's load, excess capacity, and possible non-compliance with curtailment orders.<sup>187</sup> Staff claims that Applicants offer no quantitative

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<sup>180</sup> *Id.* at 24–25.

<sup>181</sup> *Id.* at 25.

<sup>182</sup> *Id.*

<sup>183</sup> *Id.* at 22–24.

<sup>184</sup> NOVEC IB at 9, 13.

<sup>185</sup> *Id.* at 8–9.

<sup>186</sup> Staff IB at 33.

<sup>187</sup> *Id.* at 33–34; Staff RB at 24, 36.

data or detailed qualitative analysis of system benefits from the DSM Agreement.<sup>188</sup> Indeed, Staff argues, assuming Bear Island's 2005 Demand, which was lower than the DSM Agreement Demand, the DSM Agreement would provide no load control benefits to the Members.<sup>189</sup> Rather than benefiting the Members, Staff maintains that using the DSM Agreement Demand would improperly and arbitrarily shift costs among the Members.<sup>190</sup>

63. Staff further contends that the Commission policy favoring use of demand response to maintain transmission system reliability<sup>191</sup> is inapplicable in this case because Applicants do not maintain an integrated transmission system.<sup>192</sup> The policy also does not apply, according to Staff, because the Commission lacks jurisdiction over load response arrangements like the DSM Agreement.<sup>193</sup> Additionally, while Section 1252(f) of the Energy Policy Act of 2005 states a federal policy favoring demand response programs, Staff maintains that application of the provision is subject to significant state discretion.<sup>194</sup>

64. Staff attempts to rebut Applicants' reliance on *Delmarva Power & Light Co.*, 24 FERC ¶ 61,199 (1983) (*Delmarva*), and *Louisiana Public Service Commission v. Entergy Corp.*, 111 FERC ¶ 61,080 (2005) (*Entergy II*), for the point that utilities should allocate capacity costs to firm loads only—and not interruptible loads—because utilities do not need to meet the peak demands of interruptible loads.<sup>195</sup> Staff responds that the crucial factor in those cases was whether the utility had the right to interrupt the interruptible loads as needed.<sup>196</sup> In this case, Staff alleges that Applicants lack the ability to interrupt or curtail Bear Island load during non-summer months and, even during the four months

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<sup>188</sup> Staff RB at 24.

<sup>189</sup> *Id.* at 25.

<sup>190</sup> *Id.* at 28. This conclusion is based on Staff's suggestion that *all* Members may be subject to the New Dominion Tariff at stake in this proceeding and not the Settlement Rate Formulas. Staff relies on the fact that none of the Members signed onto, or was a party to, the Settlement. *Id.* at 22–23.

<sup>191</sup> See *PJM Interconnection, L.L.C.*, 99 FERC ¶ 61,139 at 61,573 (2002).

<sup>192</sup> Staff RB at 25–26.

<sup>193</sup> *Id.* at 26 (citing *New York Indep. Sys. Operator*, 98 FERC ¶ 61,268 (2002)).

<sup>194</sup> *Id.* at 27–28.

<sup>195</sup> *Id.* at 31.

<sup>196</sup> *Id.* (citing *Delmarva*, 24 FERC ¶ 61,199 at 61,462; *Entergy II*, 111 FERC ¶ 61,180 at 61,369).

when Applicants can curtail Bear Island load, the right to curtail is limited to 45 days.<sup>197</sup> Staff avers that this case also is different because Applicants do not actually treat Bear Island load as interruptible, *i.e.* they do not credit the revenues from interruptible customers to firm customers.<sup>198</sup>

65. Like NOVEC, Staff argues that, because the DSM Agreement is not part of the New Dominion Tariff, which requires use of Actual CP Demand, Applicants' use of the DSM Agreement Demand violates the filed rate doctrine.<sup>199</sup> Although Applicants have used the same practice in the past, pursuant to prior demand-side management agreements, Staff believes that failure to object in the past does not waive Staff's and NOVEC's current objections.<sup>200</sup>

66. Staff likewise objects to using Bear Island's 2005 Demand in calculating the Demand Rate going forward. Staff believes that using 2005 Demand would also violate the New Dominion Tariff, which Staff maintains requires use of *current* Actual CP Demand.<sup>201</sup> Using 2005 figures, according to Staff, also would violate cost causation principles and arbitrarily shift costs and discriminate with respect to similarly situated Member Cooperatives.<sup>202</sup>

## Applicants

67. Applicants dismiss NOVEC Witness Arsuaga's carve-out proposal as resting on the erroneous premise that the DSM Agreement harms the Member Cooperatives.<sup>203</sup> Because, absent the DSM Agreement, Bear Island's billing demand would be based on its Actual CP Demand,<sup>204</sup> Applicants assert that, to determine realistically whether the DSM Agreement shifts costs to the detriment of the Members, the correct measure is Bear

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<sup>197</sup> *Id.* at 32–33.

<sup>198</sup> *Id.* at 33–34.

<sup>199</sup> *Id.* at 29–30 (citing *Hall*, 453 U.S. at 577–78; *City of Piqua v. FERC*, 610 F.2d 950, 955 (D.C. Cir. 1979); *City of Cleveland v. FPC*, 525 F.2d 845, 854 (D.C. Cir. 1976) (*City of Cleveland*)). Staff further states Applicants' use of billing demands per the Settlement "constitutes a collateral attack on the authority of the Commission." *Id.* at 29–30.

<sup>200</sup> *Id.* at 30–31.

<sup>201</sup> *Id.* at 35 (citing Ex. ODC-4 at Original Sheet Nos. 3–6).

<sup>202</sup> *Id.* at 35.

<sup>203</sup> Applicants IB at 17.

<sup>204</sup> *Id.*

Island's Actual CP Demand during a period when there was no DSM Agreement.<sup>205</sup> The 68,000 kW demand that Mr. Arsuaga uses to show that the DSM Agreement harms the Members, the Applicants state, is merely his calculation of Bear Island's average hourly load based on historical data and has no bearing on what Bear Island's Actual CP Demand would be absent the DSM Agreement.<sup>206</sup> Applicants also dispute Mr. Arsuaga's reliance on Bear Island's statements that, since 1992, it has generally operated at 80 MW and up to 100 MW at times.<sup>207</sup> Applicants point out that, during system peak, Bear Island has regularly shed its load to 26 MW, showing that absent the DSM Agreement Bear Island's Actual CP Demand generally would not exceed 26 MW.<sup>208</sup>

68. While Applicants recognize they cannot determine what Bear Island's *future* Actual CP Demands would be absent the DSM Agreement,<sup>209</sup> they allege that a review of Bear Island's Actual CP Demand during a year when there was no agreement, *i.e.* 2005, provides a better estimate than the fictitious data relied upon by NOVEC Witness Arsuaga to show the impact of the DSM Agreement.<sup>210</sup> Applicants Witness Solomon replicated Mr. Arsuaga's calculations, using Bear Island's 2005 average monthly CP billing demand (██████ kW), instead of the 68 MW, 80 MW, and 100 MW figures used by Mr. Arsuaga.<sup>211</sup> Mr. Solomon concludes that the DSM Agreement actually benefits NOVEC, since Bear Island's Actual CP Demand in 2005 absent the DSM Agreement (██████ kW) is less than the DSM Agreement Demand (24,000 kW), causing Bear Island to pay a higher share of Applicants' costs and the other Members thus to pay a lesser share.<sup>212</sup> Specifically, Applicants state that NOVEC's power costs would *increase* by \$180,113 annually *absent* the DSM Agreement.<sup>213</sup>

69. Applicants aver the following additional benefits of the DSM Agreement: (1) New Dominion can direct Bear Island to reduce its load, which will reduce New Dominion's PJM capacity obligation and thus the amount of capacity for which the

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<sup>205</sup> *Id.* at 20.

<sup>206</sup> *Id.* at 17.

<sup>207</sup> *Id.* at 18–19.

<sup>208</sup> *Id.* at 19 (citing Ex. ODC-13 at 6–7).

<sup>209</sup> *Id.* at 20 (citing Ex. ODC-8 at 10:19–22).

<sup>210</sup> *Id.* at 21.

<sup>211</sup> *Id.* at 22.

<sup>212</sup> *Id.* at 22–23 (citing Ex. ODC-8 at 25–27; Ex. ODC-12; Exs. NVC-3 (corrected) through NVC-5 (corrected) at line 33). *See also* Applicants RB at 31, 33–34.

<sup>213</sup> Applicants IB at 22; Applicants RB at 34 (citing Ex. ODC-12 at line 16).

Members are liable;<sup>214</sup> and (2) the \$180,000 annual fee that Bear Island pays to New Dominion reduces New Dominion's costs, which are borne by the Members, and thereby reduces the Members' costs.<sup>215</sup>

70. Accordingly, Applicants ask that the undersigned Presiding Judge reject NOVEC's carve-out proposal and instead determine that NOVEC's Demand Rate should be determined using the 24 MW DSM Agreement Demand for Bear Island.<sup>216</sup> While Applicants recognize that NOVEC is not bound by the Settlement, they argue that the DSM Agreement Demand is the appropriate measure of Bear Island's demand in determining the Demand Rate to apply to all Members because: (1) Applicants have consistently used the same practice in the past;<sup>217</sup> (2) the DSM Agreement benefits all the Members;<sup>218</sup> and (3) this method comports with Commission precedent.<sup>219</sup> Applicants explain that Bear Island load in excess of 24 MW is comparable to interruptible load because Applicants can direct Bear Island to curtail down to 24 MW.<sup>220</sup> According to Applicants, under Commission precedent, "because utilities do not have to plan to meet the peak demands of interruptible loads, and it is only firm loads that cause capacity costs to be incurred, such costs should be allocated to firm loads only."<sup>221</sup> Thus, Applicants state "it would be unreasonable to allocate the Applicants' capacity costs on the basis of any amount more than the 24 MW Bear Island contract demand."<sup>222</sup>

71. In the alternative, Applicants assert that, if the Presiding Judge grants NOVEC's request to be carved out from the effects of the DSM Agreement, Bear Island's 2005 Demand is the appropriate measure of Bear Island's demand for purposes of calculating the Demand Rate in the future. As discussed *supra* P 68, Applicants maintain that Bear Island's 2005 Demand provides a more realistic measure of what Bear Island's demand

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<sup>214</sup> Applicants IB at 23–24 (citing Ex. ODC-8 at 36:10–38:7).

<sup>215</sup> *Id.* (citing Ex. ODC-9 at § 2.1).

<sup>216</sup> *Id.* at 25.

<sup>217</sup> Applicants note that NOVEC has not challenged Applicants' practice in the past of determining the Demand Rate by using a billing determinant for Bear Island that is specified in a demand-side management agreement. *Id.* at 26.

<sup>218</sup> *Id.* at 28.

<sup>219</sup> *Id.* at 28–29; Applicants RB at 39.

<sup>220</sup> Applicants IB at 28–29 (citing Ex. ODC-9 at §§ 1.1, 1.2).

<sup>221</sup> *Id.* at 29 (citing *Delmarva*, 24 FERC ¶ 61,199 at 61,462; *Entergy II*, 111 FERC ¶ 61,080 at P 16).

<sup>222</sup> *Id.*; *see also* Applicants RB at 39.

would be absent the DSM Agreement. This method, Applicants believe, best achieves NOVEC's goal of being carved out of the DSM Agreement.<sup>223</sup>

72. Applicants reject NOVEC's suggestion that Bear Island's Actual CP Demand should be used in lieu of the DSM Agreement Demand in calculating the Demand Rate. Applicants assert that because there is, and will be until 2009, a DSM Agreement in place, and the agreement alters Bear Island's behavior, using Bear Island's Actual CP Demand to calculate the Demand Rate will not achieve NOVEC's purpose of determining what Bear Island's demand would be absent the DSM Agreement.<sup>224</sup> Applicants also argue that, if Bear Island's Actual CP Demands are used, NOVEC will benefit from the DSM Agreement by paying demand charges based on Bear Island load that is curtailed pursuant to the DSM Agreement.<sup>225</sup> Such a result would be inconsistent with NOVEC's position that it should be entirely carved out from the impact of the DSM Agreement.<sup>226</sup>

73. Applicants also allege that NOVEC's argument that Applicants must use Bear Island's Actual CP Demands in calculating the Demand Rate for *all Members* constitutes a collateral attack on the Settlement. The Settlement specifies that, contrary to NOVEC's argument, *all Members other than NOVEC* will be charged a Demand Rate based on the DSM Agreement Demand for Bear Island.<sup>227</sup> Applicants further contend that NOVEC's argument violates Commission policy and precedent requiring a matching between the demand determinants used in calculating the unit charges for service and the demand determinants to which the unit charges will be applied for billing purposes.<sup>228</sup> According to Applicants, the applicable policy and precedent mean that, since the DSM Agreement requires Bear Island demand for billing purposes to be determined based on the DSM Agreement Demand, the denominator of the rate formula should likewise be based on the DSM Agreement Demand for Bear Island.<sup>229</sup>

74. Finally, Applicants argue that the DSM Agreement does not treat REC preferentially or violate principles of cost causation. In addition to repeating their belief

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<sup>223</sup> Applicants IB at 30.

<sup>224</sup> *Id.* at 32; Applicants RB at 34.

<sup>225</sup> Applicants IB at 32; Applicants RB at 34–35.

<sup>226</sup> Applicants IB at 32; Applicants RB at 34–35.

<sup>227</sup> Applicants RB at 36.

<sup>228</sup> *Id.* at 37 (citing *Kentucky Utils. Co.*, 81 FERC ¶ 61,299 at n.2 (1997); *Southern Co. Servs., Inc.*, 61 FERC ¶ 61,339 at 62,336–37 (1993); *Montaup Elec. Co.*, 38 FERC ¶ 61,252 at 61,859 (1987)).

<sup>229</sup> *Id.*

that the DSM Agreement confers benefits to the Members rather than imposing costs upon them, Applicants aver that there can be no preferential treatment toward REC because REC, unlike the other Members, has chosen to enter a demand-side management agreement with Applicants and thus is differently situated.<sup>230</sup>

75. Even if the Commission were to find that the DSM Agreement Demand cannot apply for Bear Island in calculating NOVEC's rates, Applicants reject NOVEC's carve-out proposal.<sup>231</sup> Applicants believe that resolving the differences in NOVEC's rates could be achieved through a year-end adjustment pending the completion of this proceeding.<sup>232</sup> Applicants also object to NOVEC's cascading dual-rate formulas going forward.<sup>233</sup> Applicants argue that a dual formula would be unnecessary if the rate formulas applicable to NOVEC were found to be the same as the Settlement Rate Formulas.<sup>234</sup> Even if the rate formulas were determined to be different, Applicants assert that NOVEC's proposal would require impermissible modifications of the Settlement Rate Formulas.<sup>235</sup> The only way a dual rate formula would work, according to Applicants, would be to apply the Settlement Rate Formulas first and then to collect the residual costs from NOVEC through application of the rate formula established in this proceeding.<sup>236</sup>

## B. Discussion and Ruling

76. I find that it is not unjust and unreasonable to allow Applicants to use the 24,000 kW DSM Agreement Demand for Bear Island in calculating the Demand Rate. While NOVEC and Staff show that, if Bear Island fails to curtail its load to 24,000 kW as required by the DSM Agreement, NOVEC may experience a higher Demand Rate, NOVEC and Staff fail to recognize that the Commission approved Applicants' use of the 24,000 kW demand figure when it approved the Settlement to which the DSM Agreement was attached.<sup>237</sup>

77. The fact that the Commission specifically approved an alteration to Applicants' method of calculating the Demand Rate belies the assertion that such an alteration

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<sup>230</sup> *Id.* at 38.

<sup>231</sup> Applicants IB at 14–26.

<sup>232</sup> Applicants RB at 26.

<sup>233</sup> *Id.* at 22–30.

<sup>234</sup> *Id.* at 23.

<sup>235</sup> *Id.* at 27–30.

<sup>236</sup> *Id.* at 30.

<sup>237</sup> See *New Dominion Energy Coop.*, 115 FERC ¶ 61,025.

violates the filed rate doctrine. The D.C. Circuit has stated that “[t]he considerations underlying the [filed rate doctrine]...are preservation of [FERC’s] primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.”<sup>238</sup> Here, the Commission clearly was cognizant in the change in Applicants’ inputs into their Demand Rate Formula since the change was part of the Settlement filed with, and approved by, the Commission. The concerns behind the filed rate doctrine thus do not pertain here.

78. Moreover, contrary to Staff’s suggestions, all eleven Members other than NOVEC are bound by the Settlement. Applicants are cooperatives whose boards are run by the Members and have authority to bind all Members.<sup>239</sup> By signing the Settlement, Applicants thereby bound all New Dominion Members, with the exception of NOVEC who the Commission specifically excepted in the Settlement Order. It also should be noted that none of the Members other than NOVEC objected to the Settlement. The Settlement Order stated that a hearing would be held to examine NOVEC’s rate issues, not to determine the rates applicable to the other eleven Members. Accordingly, any objections to the DSM Agreement based on its impact on Member Cooperatives other than NOVEC lack merit since those Members, through Applicants, specifically agreed to the terms of the Settlement and its attachments, including the DSM Agreement.

79. With respect to NOVEC, in approving the Settlement, the Commission has considered and rejected NOVEC’s concerns about the DSM Agreement increasing NOVEC’s rates. In the Settlement Order, the Commission summarized NOVEC’s objections to the Settlement as follows:

[The Settlement] contains changes to the Old Dominion and New Dominion rate formulas that will harm NOVEC because the settlement enables Bear Island to avoid certain cost responsibilities for which NOVEC would be largely responsible. NOVEC argues that the combination of the rate formula revisions and the proposed demand side management agreement provides substantial benefits to Bear Island and little or no apparent benefit to Old Dominion and its members, and will cause the members to bear the cost of the benefits being bestowed upon Bear Island.<sup>240</sup>

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<sup>238</sup> *City of Cleveland*, 525 F.2d at 854.

<sup>239</sup> While the Settlement Order did not specifically state this, it is the only logical conclusion. If the eleven Members, other than NOVEC, were not bound by the Settlement, it is unclear to whom the Settlement Rate Formulas would even apply.

<sup>240</sup> *New Dominion Energy Coop.*, 115 FERC ¶ 61,025 at P 5.

The Commission found that NOVEC had raised no genuine issues of material fact.<sup>241</sup> Although the Commission found that the Settlement does not apply to NOVEC,<sup>242</sup> the Commission did not suggest that NOVEC should be entirely insulated from any impact of the terms of the Settlement. NOVEC's concerns about the residual impact of the DSM Agreement have been considered and rejected by the Commission. Moreover, Applicants state, and NOVEC does not refute, that ensuring that NOVEC experiences no impact from the implementation of the Settlement and accompanying DSM Agreement would require modification of the Settlement Rate Formulas.<sup>243</sup> The Settlement Order accepted the Settlement Rate Formulas in full, as applied to the Members other than NOVEC, and did not contemplate later revision to ensure NOVEC was not impacted by the Settlement.

80. Staff and NOVEC's argument that the DSM Agreement gives REC preferential treatment also lacks merit. As Applicants note, REC's customer—Bear Island—is a party to a demand-side management agreement with Applicants. Presumably, customers of the other Member Cooperatives are free to negotiate similar contracts with Applicants and thereby obtain any alleged benefits that REC obtains through the DSM Agreement.

81. I also reject NOVEC's argument based on principles of cost causation. The cases cited by NOVEC collectively stand for the proposition that "rates should produce revenues from each class of customers which match, as closely as practicable, the costs to serve each class or individual customer."<sup>244</sup> The D.C. Circuit in *Alabama Electric*, however, also stated that "[i]t would no doubt be impossible, even if desirable, to formulate a rate scheme with such precision that each customer...is made to bear the exact cost of the service he received."<sup>245</sup> Applicants' use of the 24 MW figure as Bear Island's billing demand to calculate the Demand Rate represents a reasonable attempt to match costs to their source. Applicants offer uncontested evidence that Bear Island, in the past, has been able to shed load to 26 MW or less during system peak.<sup>246</sup> Based on that history, it is reasonable to conclude that Bear Island will be able, consistent with the DSM Agreement, to shed load to 24 MW during system peak. If Bear Island does shed load to 24 MW, the DSM Agreement Demand used for Bear Island in determining the Demand Rate will be consistent with the costs actually caused by Bear Island.

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<sup>241</sup> *Id.* at P 10.

<sup>242</sup> *Id.* at P 12.

<sup>243</sup> *See Id.* at P 11.

<sup>244</sup> *Alabama Electric*, 684 F.2d at 28–29.

<sup>245</sup> *Id.* at 26. Indeed, in the *KN Energy* case cited by NOVEC, the court held that FERC could even temporarily forego the cost-causation analysis to resolve a "take-or-pay" problem. *KN Energy*, 968 F.2d at 1301.

<sup>246</sup> *See supra* P 68 (noting that Applicants' 2005 demand was [REDACTED] kW).

82. Accordingly, I find that Applicants' current method of calculating and applying the Demand Rate to all Member Cooperatives is just and reasonable and reject NOVEC's proposed dual-rate formula going forward and carve-out proposal for the current year's rates.

**Issue 7: Is Applicants' interpretation of the Prior Period Adjustment for Demand Revenues provision of the New Dominion Tariff arbitrary and capricious?**

**A. Positions of the Parties**

**Staff**

83. Staff argues that Applicants' interpretation of the proposed tariffs is arbitrary and capricious because Applicants plan to use the Prior Period Adjustment for Demand Revenues Provision (PPA Provision) of the New Dominion Tariff to recover any under-recoveries that they may experience as a result of the Settlement.<sup>247</sup> In pertinent part, the PPA Provision reads: "Any differential between allowed demand costs collected under the formula and actual demand costs incurred for the period is allocated to each [Member] based on actual demand billing units and, unless the Board of Directors decides otherwise, is refunded or collected from each [Member] within the following calendar year."<sup>248</sup> Staff emphasizes the language "unless the Board of Directors decides otherwise." Specifically, Staff appears concerned about Applicants using the PPA Provision to recover shortfalls in their recovery of costs that may result from: (1) use of the DSM Agreement Demand for Bear Island in calculating the Demand Rate;<sup>249</sup> and (2) differences between the New Dominion Tariff and the New Dominion Settlement Tariff in terms of the classification of Account 553<sup>250</sup> and the applicable Reactive Power Rate.<sup>251</sup>

84. According to Staff, using the PPA Provision in that manner is contrary to its plain meaning and purpose.<sup>252</sup> Staff avers that the PPA Provision serves to true-up or adjust differences between actual demand costs and allowed demand costs, which are estimated

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<sup>247</sup> Staff IB at 17 (citing Tr. at 354:7–25, 368:3–17, 376:22–377:20; Ex. ODC-4 at Original Sheet No. 10).

<sup>248</sup> Ex. ODC-4 at Original Sheet No. 10.

<sup>249</sup> See *supra* Issue 6.

<sup>250</sup> See *supra* Issue 2.

<sup>251</sup> See *supra* Issue 5.

<sup>252</sup> Staff IB at 17.

under the rate formula in the New Dominion Tariff.<sup>253</sup> The PPA Provision is not meant to adjust differences between the Settlement Tariffs and the New Dominion Tariff.<sup>254</sup> Such a use of the PPA Provision, Staff contends, would allow Applicants to change rates without notice to ratepayers and without Commission review.<sup>255</sup> Staff warns that, because the New Dominion Tariff does not require Applicants, when recovering shortages resulting from the Settlement Tariff, to assess the Members separately or to make a rate filing, Applicants could indiscriminately pass through to the Members costs unrelated to the services rendered.<sup>256</sup>

## Applicants

85. Applicants aver that their interpretation of the tariffs is not arbitrary and capricious. The PPA Provision allows Applicants to collect their costs fully by truing up differences between actual and estimated demand-related costs. Absent the PPA Provision, Applicants allege that Old Dominion would have to file a rate case every year to seek approval of its matching of expenses to revenues.<sup>257</sup>

86. Applicants opine that Staff's concerns with the PPA Provision result from a misunderstanding of the nature of a cooperative.<sup>258</sup> Applicants maintain that they do not use the PPA Provision indiscriminately to pass through to Members costs unrelated to the services the Members receive.<sup>259</sup> Rather, adjustments under the PPA Provision are made in accordance with a prescribed formula.<sup>260</sup> Applicants note that Old Dominion's rate formulas have included a PPA Provision for many years, with no evidence of abuse or misuse.<sup>261</sup> Moreover, Member representation on the New Dominion Board mitigates against efforts to over-recover or cover excessively for under-recoveries of costs.<sup>262</sup> According to Applicants, the PPA Provision does not give the New Dominion Board unlimited discretion. The language "unless the Board of Directors decides otherwise" merely gives the Board discretion with respect to the timing for exercising the PPA

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<sup>253</sup> *Id.* at 18 (citing Tr. at 348:12–349:4, 350:3–351:14).

<sup>254</sup> *Id.*

<sup>255</sup> *Id.* at 19.

<sup>256</sup> *Id.* (citing Tr. at 355:1–15).

<sup>257</sup> Applicants RB at 20.

<sup>258</sup> *Id.* at 18.

<sup>259</sup> *Id.* at 17.

<sup>260</sup> *Id.* at 16–17.

<sup>261</sup> *Id.* at 20.

<sup>262</sup> *Id.*

Provision and is not meant to give Applicants discretion to use a different method of allocating expenses and revenues.<sup>263</sup>

87. Applicants note that Staff has no proposed solution to the alleged problem with the PPA Provision.<sup>264</sup> Accordingly, Applicants request that the undersigned Presiding Judge find that the Applicants' application of the PPA Provision is not arbitrary and capricious.

## **B. Discussion and Ruling**

88. Because under the rulings made in this Initial Decision there will be no difference between the New Dominion Tariff and the New Dominion Settlement Tariff, the DSM Agreement is the only matter that gives rise to possible under- or over-collection of costs. Because this Initial Decision rejects Staff's and NOVEC's challenges to the DSM Agreement and its relationship to the filed tariffs,<sup>265</sup> it is now up to Applicants to determine the proper method of recovering any under- or over-recoveries of costs that may result from the implementation of the DSM Agreement. Applicants note that they have never been accused in the past of abusing the PPA Provision. Staff provides no evidence to the contrary and provides no reason to believe Applicants will abuse the provision in the future. Accordingly, I find that Staff has not shown that Applicants' interpretation of the filed tariffs is arbitrary and capricious. Even if Staff had proven its point, Staff suggests no viable solution to the alleged problem with the PPA Provision. As Applicants note, and Staff recognizes, the PPA Provision provides Applicants an important tool for properly matching expenses to revenues. Presumably, Staff would not suggest the PPA Provision be removed from the New Dominion Tariff, but short of that it is unclear what remedy Staff would recommend.

## **Issue 8: Must changes to Applicants' rate formulas be made to accommodate prospective changes in NOVEC's WPC?**

### **A. Positions of the Parties**

#### **NOVEC**

89. NOVEC contends that the Commission's March 8 Order requires a determination as to whether Applicants' rate formulas should be changed in order to accommodate "to-be-revised WPCs."<sup>266</sup> NOVEC clarifies that it "has not asserted that the WPCs must be

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<sup>263</sup> *Id.* at 20–21.

<sup>264</sup> *Id.* at 21.

<sup>265</sup> This is in addition to the Commission having rejected essentially the same arguments in the Settlement Order.

<sup>266</sup> NOVEC IB at 24; Ex. NVC-1 at 6:16.

modified as a part of this proceeding.”<sup>267</sup> Rather, NOVEC explains that certain adjustments must be made to Applicants’ budgeting and cost allocation process “to ensure proper cost allocation where one or more members is operating under a revised WPC, and [that this] can be done in such a way that properly allocates costs among the members whether or not the WPC’s are modified now or later.”<sup>268</sup>

90. Citing the testimony of its Witness Arsuaga, NOVEC argues that Applicants need to address three areas: (1) To identify the existing power requirements of each of the Members to allow Members to participate in some but not all projects; (2) to adjust the budgeting process to provide for multiple budgets—one for Members’ existing power requirements and one for new power supply projects; and (3) to devise new formula rates, once the new projects come on line, to allocate costs of new projects to the Members based on their participation in those projects.

91. NOVEC contests Applicants’ position that specific changes to the existing WPCs must be known before any revisions can be made to the budgeting and cost allocation process. According to NOVEC, the Commission ordered that the cost allocations under the “to-be-revised” WPCs be addressed in this proceeding regardless of the uncertainty of revised contract terms. NOVEC points out that Applicants passed a Board resolution committing to negotiate new WPCs with one or more members after the reorganization proceedings are complete. NOVEC interprets this resolution to mean that renegotiation of the WPCs *to allow for a partial requirements contract* is a certainty.

92. NOVEC contends that contrary to Applicants’ view, the Commission’s denial of NOVEC’s complaint in Docket No. EL06-43-000 seeking renegotiation of its WPC does not foreclose revisions to the WPC. NOVEC reiterates that Applicants have committed to negotiating revisions to the WPCs.<sup>269</sup> In its Reply Brief, NOVEC insists that the three modifications to Applicants’ rate formulas supported by Witness Arsuaga do not require knowing what the specific terms of the revised WPC will be except that the revised WPC will be a partial requirements contract.<sup>270</sup>

93. NOVEC also argues that Applicants have made no effort to prove that NOVEC’s proposed modifications are unjust or unreasonable or cannot be implemented.<sup>271</sup> NOVEC contends that it is reasonable to require Applicants “as part of their compliance

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<sup>267</sup> NOVEC IB at 25.

<sup>268</sup> *Id.*

<sup>269</sup> *Id.* at 28.

<sup>270</sup> NOVEC RB at 29.

<sup>271</sup> *Id.* at 31.

filings, to modify their budgeting and allocation process to ensure proper cost allocation where one or more members is operating under a partial-requirements WPC.”<sup>272</sup>

### Applicants

94. Applicants contend that it is “impossible to prepare at this time a new rate formula that will satisfy the requirements of ‘not yet revised’ WPCs.”<sup>273</sup> Applicants argue that this proceeding concerns whether rate formulas they propose are just and reasonable and not unduly discriminatory. According to Applicants, testimony on proposed rate formula changes based on a yet to be revised WPC is irrelevant.

95. To support their irrelevance argument, Applicants rely, in part, on the Commission’s recent rulings in Docket No. EL06-43 denying NOVEC’s complaint and request for rehearing with respect to renegotiating its WPC.<sup>274</sup> Applicants argue that, in Docket No. EL06-43, the Commission has concluded that NOVEC is bound by the terms and conditions of the current WPC and has rejected NOVEC’s unilateral effort to force changes. In Applicants’ view, NOVEC’s WPC can be modified only if the parties to the contract, including Old Dominion, consent to modification in writing. Applicants point out that Old Dominion has not consented, and without such consent there is no basis for concluding that NOVEC’s WPC will be revised according to its specifications.

96. Applicants also cite the undersigned Presiding Judge’s bench ruling on July 8, 2005 that the hearing in this case implicates only the WPCs in their current form and “does not encompass the question of renegotiation of the WPC between NOVEC and Old Dominion and New Dominion....”<sup>275</sup> Applicants aver that even NOVEC Witness Arsuaga admitted on cross-examination that his testimony is wholly intended to contemplate a revised, partial-requirements WPC and not the WPCs in their current form.<sup>276</sup>

97. Applicants further contend that NOVEC seeks to have the rate formulas modified in these proceedings to accommodate a revised, partial-requirements WPC that does not

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<sup>272</sup> *Id.* at 32.

<sup>273</sup> Applicants IB at 50.

<sup>274</sup> See *Northern Va. Elec. Coop., Inc. v. Old Dominion Elec. Coop.*, 114 FERC ¶ 61,240, *reh’g denied*, 116 FERC ¶ 61,173 (2006) (*NOVEC*).

<sup>275</sup> Applicants RB at 54 (quoting Order Following Oral Argument Denying Consolidation and Addressing the Scope of the Issues, Docket Nos. ER05-18-002, ER05-309-002, at P 3 (July 8, 2005)).

<sup>276</sup> *Id.*; Applicants IB at 48–49.

currently exist.<sup>277</sup> As such, any change to the formula rates to accommodate a change in the WPCs is entirely speculative and therefore unjust and unreasonable. Applicants urge the undersigned Presiding Judge to find that the rate formulas are just and reasonable in the sense that they accommodate the current WPCs and that pursuing NOVEC's proposed changes at this time would render the rate formulas unjust and unreasonable.

## B. Discussion and Ruling

98. I agree with Applicants that the issue of a possible revised WPC between NOVEC and Applicants is not part of this case. The Commission's reference to the "yet to be revised WPCs" in its March 8 Order merely refers to Applicants' apparent acquiescence at that time to possible revisions of their WPC with NOVEC. Subsequently, no revisions to the WPC have been made regardless of NOVEC's repeated attempts to force the issue. Furthermore, as Applicants maintain, the Commission has denied NOVEC's efforts to compel Applicants to renegotiate their WPC.<sup>278</sup> NOVEC's arguments about rate changes to accommodate a revised WPC are therefore speculative.

99. Although NOVEC seems confident that any revised WPC will provide for a partial requirements contract, it offers no grounds for such an assumption, and, as far as the record shows, Applicants have never agreed to a partial requirements contract with NOVEC or any other Member. Since none of Applicants' Members currently have a partial-requirements WPC, there is no valid reason to require Applicants to change their rate formulas to take into account the *possibility* that such a WPC will be negotiated in the future. Moreover, NOVEC has failed to show that Applicants' rates are unjust and unreasonable *because* they currently do not take into account the possibility that partial requirements contracts may be negotiated in the future.

## III. Order

100. It is ordered that subject to review on exceptions or on the Commission's own motion, as provided in the Commission's Rules of Practice and Procedure, within thirty (30) days of the issuance of the Final Order of the Commission adopting the Initial Decision in this proceeding, all parties shall take the appropriate action to implement the rulings in this decision.

Judith A. Dowd  
Presiding Administrative Law Judge

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<sup>277</sup> Applicants RB at 53-54.

<sup>278</sup> See *NOVEC*, 114 FERC ¶ 61,240, *reh'g denied*, 116 FERC ¶ 61,173.