APPENDIX C

Furthermore, to the extent ITC relies on the Fama-French methodology rather than DCF analysis, it is collaterally attacking Order 679 — ironically, the very order on which ITC relies in seeking above-cost rates. In that rulemaking, numerous commenters "request[ed] that the Commission adopt additional methodologies, such as risk premium, comparable earnings, Fama-French, and/or capital asset pricing, to use along with the current DCF analysis because a multiple model approach will result in a more representative ROE range." Order 679 at P 99. The Commission rejected those requests, concluding that "Our past practice of using the DCF approach has yielded just and reasonable results and is consistent with long-standing ratemaking principles." *Id.* at P 102.

This ruling was correct. The DCF approach yields just and reasonable results here as well, by demonstrating that the high end of the zone of reasonableness does not extend above the currently-applicable 12.38% ROE.

(5) Summary of DCF Results

In its May testimony, ITC has presented (as Table 1, Exh. IT-4 at 6) a "Summary of DCF Estimation Results: Midwest ISO Group." It equates the "zone of reasonableness" with the range of individual ICOEs in each DCF study, and is meant to make 13.88% look reasonable by extending higher. A similar table, with the same intention but more detail, has also been presented in Exh. IT-4, Schedule 8. But a revised version of either table, incorporating the corrections shown above to be necessary, demonstrates that the requested 13.88% is far above the zone of reasonableness.

Summary of Corrected DCF Estimation Results: Midwest ISO Group

DCF Model	Zone of reasonableness
FERC: DCF-Electric	6.77%-11.96%
Quarterly DCF	8.37%-12.08%

Quarterly DCF + FERC Stock Prices 8.45%-12.34%

Exh. IT-4, Schedule 8, Revised:
Summary of Analysis Results for MISO Group Utilities

Company	FERC DCF Low	FERC DCF High	QDCF	QDCF + FERC Stock Prices
Allete Inc.	8.16%	9.95%	9.02%	9.18%
Alliant Energy	7.90%	9.24%	8.37%	8.45%
DTE Energy	6.76%	10.43%	9.60%	9.75%
Duke Energy	7.19%	10.73%	12.08%	12.34%
MDU Resources	9.16%	11.96%	10.00%	10.08%
Otter Tail	7.55%	8.91%	8.37%	8.58%
Vectren	7.00%	8.58%	8.60%	8.64%
Xcel Energy	8.05%	10.36%	9.86%	10.11%
Average	**8.87%**		**9.49%**	**9.64%**
Minimum	**6.76%**		**8.37%**	**8.45%**
Maximum	**11.96%**		**12.08%**	**12.34%**
Median	**8.74%**		**9.31%**	**9.47%**
Midpoint	**9.36%**		**10.23%**	**10.40%**

A 13.88% return would be off both charts, and should be out of the question.

c) ITC's Conclusory Assertion that Transmission Is Riskier than Competitive Operations Is Both False and Estopped

What ITC tells its investors and the story that it attempts to sell to this Commission are strikingly different. According to the most recent ITC Holdings prospectus, ITC is an exceptionally predictable, safe investment:

> *Predictability.*
>
> We believe that the following elements make our performance more predictable than other regulated businesses:
>
> - formulaic rate setting mechanism;

> - no rate hearings required to adjust rates; and
> - rates adjusted annually to reflect recent capital investment.
>
> In addition, we believe that the following strengths, when combined with our growth strategy and predictable performance, provide us with an opportunity for growth:
>
> - *Supportive Regulatory Environment for Independent Transmission Companies;*
> - *Lower Risk, Less Contentious Capital Investment Largely Focused on Rebuilding and Upgrading Existing Transmission Equipment;*
> - *Minimal Commodity and Energy Demand Risk;*
> - *Attractive Service Territories;*
> - *Lack of Competition; and*
> - *Experienced Management Team.*

ITC Prospectus at 105-106. But that, of course, is what ITC tells people when it wants their investment dollars. When it wants this Commission to authorize it to pocket extra dollars from consumers, it claims that ITC is somehow made riskier by the fact that "100% of ITC's revenues, including revenues from ITC Midwest, will be from regulated transmission operations, whereas all of the other Midwest ISO utilities derive significant revenues from unregulated operations." Exh. IT-4 at 45; see also Application at 42 ("ITC Midwest … will lack the larger, more diversified rate base of a traditional, vertically integrated public utility company"). On Wall Street, "minimal commodity and energy demand risk" make ITC low-risk; here, ITC would have the Commission believe that vertical separation from those risks makes ITC risky.

Let's be serious: the Wall Street version is the true one. (In any case, that is what Wall Street thinks, and that ultimately is what matters in determining the cost of equity.) For example, the most recent Standard & Poors Research Update for ITC does not mince words:

> ITC Transmission and METC benefit from being sole providers of electricity transmission service to Detroit Edison Co. (BBB/Stable/A-2), Consumers Energy Co. (BB/Stable/--), and numerous cooperatives and municipal utilities. The inclusion of

> transmission assets in Iowa, Minnesota, and Illinois should help further geographically diversify Holdings' revenues and cash flows and broaden its customer base. Moreover, there is minimal competitive risk because of high regulatory and political barriers to entry.
>
> Prospectively, although integration risk would remain, the added customer, economic, and geographic diversity provided by this acquisition would further support Holdings consolidated business risk profile. The business risk profile is scored a '2' (excellent). (Business profiles are categorized from '1' (excellent) to '10' (vulnerable)). The excellent business risk profile reflects very supportive regulation, minimal operating risk, and increasingly diversified markets and customers offset by Holdings' aggressive growth and exposure to weather-related demand variability.

Standard & Poor's, *ITC Holdings And Units 'BBB' Rating Affirmed After Acquisition Announcement* (Jan. 17, 2007).

In short, Wall Street views ITC's transmission-oriented business profile as reducing risk, not increasing it. As the Fitch rating agency recently observed, "From a credit perspective, Fitch views investments in the transmission sector as being relatively low risk compared to similar investments on the generation segment based on current supportive regulation and low operating risk." FitchRatings, *U.S. Power Transmission Projects: Less Candy?* (Apr. 2, 2007).

And the Commission has so found. In *City of Vernon, California*, Opinion No. 479, 111 F.E.R.C. ¶ 61,092, P 101 (2005), *clarified,* 112 F.E.R.C. ¶ 61,207 (2005), *reh'g denied*, 115 F.E.R.C. ¶ 61,297 (2006), the Commission concluded that "Vernon's transmission operations are not riskier than the composite operations of the companies in the proxy group which are involved in riskier unregulated business and competitive generation operations." Similarly, in *Bluegrass Generation Company, L.L.C.*, 118 F.E.R.C. ¶ 61,214, P 86 (2007), the Commission found that "an interconnected utility's return is a conservative estimate of a merchant generator's return because the merchant generator faces more risk." More generally, the Commission has long recognized that a company's focus on one line of safe business makes that company safer, not riskier, than a company that conducts that safe line plus riskier lines. *See Yankee Atomic Elec. Co.*, 40 F.E.R.C. ¶ 61,372, 62,206-07 (1987), *reh'g denied*, 43 F.E.R.C. ¶ 61,2323, *on remand*, 47 F.E.R.C. ¶ 61,258 (1989). ITC's litigation-only spin — that abstaining from risky generation investments makes it riskier — is not only contrary to its Wall Street statements and illogical, it is also foreclosed by precedent.

Indeed, ITC and Alliant are estopped from claiming that transmission is riskier than generation or than vertically-integrated operations in the aggregate. ITC, Alliant, and the other MISO TOs presented essentially the same argument in the Docket No. ER02-485 proceeding in which the still-applicable 12.38% return was set. On that basis, they contended for a 13.0% ROE, above the 12.38% midpoint of the Midwestern utilities proxy group presented there. But the Initial Decision found that "the purported risks of transferring transmission assets to the MISO" were "highly speculative," such that the midpoint of the Midwestern utilities proxy group amply compensated for transmission risks. *Midwest ISO ROE Initial Decision* at P 76 & n.42. It also found (over the objections of some of the members of the Municipal Coalition, and other stakeholders) that a proxy group comprised of numerous vertically-integrated Midwestern utilities fairly represented the risks and costs of equity capital invested in transmission, such that looking instead to a smaller number of wires-only proxies was inappropriate. *Id.* at PP 18, 22. The Commission affirmed on both points. *Midwest ISO*, 100 F.E.R.C. ¶ 61,292, PP 12, 30-31 (2002), *aff'd in part*, *Pub. Serv. Co. of Ky. v. FERC*, 397 F.3d 1004 (2005), *on remand*, 111 F.E.R.C. ¶ 61,355 (2005).

These rulings established the basis on which IPL secured the still-applicable 12.38% MISO-wide return that ITC and Alliant seek to use as a springboard to even more lucrative returns. But even while attempting that leap, ITC and Alliant are now asserting that the essential premise underlying that 12.38% — that the publicly-traded parents of MISO-participating utilities provide a reasonable, comparable-risk proxy group for inferring the relevant cost of equity — was wrong after all. *But see ComEd.,* 119 F.E.R.C. at PP 78-79; *TrAIL,* 119 F.E.R.C. at P 40.

d) The 13.88% that ITC's Southeast Michigan Affiliate Secured Through Historical Accident Does Not Support ITC Midwest's Present Claim

Alongside its fatally-flawed empirical studies, ITC makes an argument that any parent will recognize: "But you gave me an extra dessert that one time — can I have some tonight?" ITC asserts that its "requested ROE of 13.88% is based on the 12.38% Midwest ISO ROE, and includes 50 basis points for ITC Midwest's participation in the Midwest ISO and 100 basis points for the independent ownership of ITC Midwest," thereby adding up to "the ROE that the Commission accorded to ITC*Transmission.*"[75]

But this plea is no basis for an end-run around the empirical data, which as demonstrated above show that 13.88% is far above the current reasonable range. Whether it is arrived at by adding a generic bonus to the existing ROE or by an approach that is actually tailored to its risks and circumstances, any ROE awarded here must be kept within a range that is found to be reasonable based on substantial evidence in this case, *i.e.,* based on current empirical data. Order 679-A is quite clear on this point:

> Generic adders, as recommended by Southern Companies, would still require the Commission to make a determination that the proposed ROEs are just and reasonable, and its findings would have to be based on reasoned decision-making. Therefore, the

[75] Application at 41. ITC*Transmission* is ITC Midwest's Southeast Michigan affiliate, which owns transmission facilities previously owned by The Detroit Edison Company.

> Commission necessarily would be required to establish a zone of reasonableness and a justification for the approved ROEs.

Order 679-A at P 64.

Reasoned decision-making as to the currently reasonable zone requires a basis in substantial evidence as to equity's current cost. "A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally." *Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm'n of W. V.*, 262 U.S. 679, 693 (1923). Accordingly, reliance on the rate of return set in a prior proceeding "might be permissible" only where "pertinent local conditions and economic conditions generally have remained static during the intervening years," and "the risk factor, so important an element in fixing rate of return, has remained static." *Washington Gas Light Co. v. Baker*, 188 F.2d 11, 17 (D.C. Cir. 1950). The outcome here is controlled by the D.C. Circuit's longstanding doctrine that any change in the rate of return must be supported by a record reflecting current conditions: "Since the Commission's findings and conclusions <u>must be based on a record reflecting current conditions</u>, it is neither required nor permitted to give conclusive weight to past return allowances or to treat dividend payouts of prior years as a matter of right."[76] *See generally Cent. Me. Power Co. v. FERC,* 252 F.3d 44 (1st Cir. 2001) (Commission is "not entitled to ignore claims that [a cost] ... is less than it was in the past").

In short, current financial market data cannot be ignored when considering the proposed massive rate increase for the transmission service that the Midwest ISO will continue to provide in its eastern Iowa zone. To ignore the current data would not be consistent with the judicially-enforceable requirements of reasoned decisionmaking. And as discussed in Part II.A.2.a) above,

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[76] *Payne v. Washington Metropolitan Area Transit Comm'n.*, 415 F.2d 901, 914 (D.C. Cir. 1968) (emphasis added; citations to Federal Power Act and other cases omitted).

the current data are conclusive that there is no headroom in the zone of reasonableness to increase the rate of return above the currently-applicable 12.38%, much less to raise it to 13.88% as ITC desires.

Furthermore, even if current reality could be ignored, ITC has not explained why it should have a special right to a 50 basis point bonus for MISO participation that is accorded to neither its sibling MISO participants, such as IPL, nor to ITC's most recent operating company, METC. The incentive awarded to what is now ITC*Transmission* was not the 150 basis points that ITC Midwest seeks here, but rather "100 basis points above that approved by the Commission for participation in the Midwest ISO." *ITC Holdings Corp.*, 102 F.E.R.C. at P 63. By historical accident, ITC*Transmission* was able to lock in its 13.88%, as 12.88% plus 100 basis points, when the MISO-wide ROE was erroneously in effect as 12.88%. But that was before the D.C. Circuit reversed the 12.88% as unfair, and the MISO-wide ROE was set as 12.38%.[77] ITC's other Michigan affiliate, the Michigan Electric Transmission Company, has a 13.38% approved ROE precisely because it was established as 12.38% plus 100 basis points, after the D.C. Circuit reversal. *Mich. Elec. Transmission Co., LLC,* 113 F.E.R.C. ¶ 61,343 (2005), *reh'g granted in part*, 116 F.E.R.C. ¶ 61,164 (2006). After and based on this reversal, the Commission specifically held that METC was not eligible for a 50 basis point bonus for RTO participation. *Id.* at P 15.

To be sure, the Commission has not prohibited an application by MISO TOs for an RTO participation incentive, and the rejection of METC's request for 50 extra points was "without prejudice to Michigan Electric participating in a proposal to adopt an ROE adder for RTO

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[77] *Pub. Serv. Comm'n of Ky. v. FERC,* 397 F.3d 1004 (D.C. Cir.) ("*PSCKY*") (now-Chief Justice Roberts) (vacating 50 basis point incentive for RTO participation), *on remand,* 111 F.E.R.C. ¶ 61,355 (2005) (adopting 12.38% as the

participation in a proceeding addressing the ROE applicable to all Midwest ISO transmission owners." *Id.* But MISO TOs have not submitted such an application, here or elsewhere, and for good reason. They undoubtedly are aware that under Order 679 and related case law, any incentive-heightened total return must be kept within a zone that is currently reasonable. They also must know that the 12.38% they now enjoy is far above current equity costs, as shown in Part II.A.2.a) above. The MISO-wide ROE record in Docket No. ER02-485 reflected a passing, and now long-past, electric utility stock price crash in the wake of the Enron and California meltdowns. It also reflected application of the 12.38% midpoint, rather than the 50-basis-points-lower median of 11.88%, as a special rate for that RTO-wide context. And perhaps most significantly, it reflected in that midpoint the highest (by far) ICOE in that record, a 15.96% ICOE-high for Aquila, *a.k.a.* Utilicorp. That company was then expected to participate in the Midwest ISO, but ultimately did not. It therefore would be excluded from the proxy group if the MISO-wide ROE were re-litigated today. Presumably for the same reason, its deletion is the only membership difference between Dr. Lesser's eight-utility proxy group and the nine-utility proxy group relied upon in that case. Without that proxy, the midpoint of the other ICOEs found in the MISO case was 11.85%. In short, were MISO TOs to seek an explicit RTO-participation adder, the existing 12.38% base level would be wide open to re-examination on multiple grounds.

The longstanding "integral part" doctrine holds that the reasonableness of an upwards adjustment to one rate component must be considered in the context of the overall existing rates, which are thereby opened to investigation. *See Colo. Interstate Gas Co. v. FERC*, 791 F.2d 803 (10th Cir. 1986); *Cities of Batavia v. FERC*, 672 F.2d 64 (D.C. Cir. 1982) (Commission must

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cost-based, MISO-wide ROE, while providing for future Section 205 filings to consider adding incentives while also review "a revised rate completely to assure that all its parts — old and new — operate in tandem to insure a 'just and reasonable' result"); *N. Border Pipeline Co.,* 89 F.E.R.C. ¶ 61,185 (1999). This doctrine has recently been followed in a closely analogous case. When New England TOs sought ROE heighteners in RTO transmission rates, the Commission did not allow any bonus without simultaneously revisiting the cost-based ROE component. That component turned out to be 10.2%, significantly <u>below</u> the previously prevailing level of 11%. Consequently, the Commission established the incentivized ROE level for existing high-voltage facilities as 10.7% (*i.e.,* the updated 10.2% level plus 50 basis points for RTO participation), <u>not</u> as 11% plus 50 basis points. Note also that this 50 basis point RTO participation bonus applied only to the higher-voltage "RNS" portion of the New England TOs' transmission rate base, and as such was significantly more limited in both scope and quantity than ITC's request — which seeks 150 basis points added to all of its facilities, including existing 34 kV ones.

In short, the continuation of the 12.38% standard MISO ROE is collecting more than current costs, and as such it already includes a substantial effective bonus for continued RTO participation. Indeed, the Initial Decision underlying this existing return level found that "this ROE (an increase from the then-current ROE of 10.5%) sufficiently covers the possibility of any additional risks and the higher return should provide sufficient incentive for investment, addressing the concerns raised by the MISO and the MISO TOs (this return should not hinder the expansion of the RTO)." *Midwest ISO ROE Initial Decision* at P 77. ITC Midwest has provided no justification for awarding it a special, further bonus for RTO participation that the American Transmission Company, METC, IPL, and other MISO TOs do not receive.

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potentially reconsidering the cost-based component in light of updated capital market information).

3. Capital Structure

Consistent with the low business risk its operating companies enjoy, ITC Holdings is quite leveraged. As of January 2007, "Debt to total capital was 70.3%, up from 68.5% as of June 30, 2006. Standard & Poor's expects leverage to remain around 70%, as indicated by Holdings." Standard & Poor's, *ITC Holdings And Units 'BBB' Rating Affirmed After Acquisition Announcement* (Jan. 17, 2007). S&P is correct: According to its Annual Report to Shareholders for 2006, ITC Holdings' capital structure includes $0.532 billion in total equity and $1.262 billion in long-term debt, which translates to an approximately capital structure consisting of approximately 30% equity, 70% debt. The debt, of course, costs relatively little in today's environment of historically low interest rates:

Entity	$ (millions)	Share of Debt	Interest Rate
ITC Holdings	$267.0	22%	5.25%
ITC Holdings	$255.0	21%	5.875%
ITC Holdings	$255.0	21%	6.375%
ITC*Transmission*	$185.0	15%	4.45%
ITC*Transmission*	$100.0	8%	6.125%
METC	$175.0	14%	5.75%
Consolidated	$1,237.0	100%	5.63%

ITC Holdings' leveraged structure is not intended to change much after an acquisition of IPL's facilities. According to the January 2007 S&P report, "Funding for the acquisition is expected to include a mix of debt and equity in line with Holdings' current capital structure. We estimate that the acquisition of Alliant's transmission assets could increase Holdings' consolidated debt by approximately $525 million based on its 70% debt leverage target." Exh. IT-4, Schedule 5, page 2 likewise shows the capital structure of ITC Holdings as being 70.3%

long-term debt, 29.7% common equity (and no preferred stock). Nor is significant change expected in the cost of long-term debt.[78]

Because ITC Holdings owns 100% of its operating subsidiaries, that highly leveraged capital structure is the only capital structure that equity investors see. Thus, even if the actual cost of equity capital to ITC Holdings is 12.38% — and there is substantial reason to doubt that it is that high, see Part II.A.2.a) above — the consolidated actual cost of capital for ITC would be only 7.64%:

Component	Share of Cap. Structure	Return per above	Weighted Return
LT Debt	70.30%	5.63%	3.96%
Equity	29.70%	12.38%	3.68%
Cost of Total Capital			7.64%

With a 13.88% heightened ROE substituted for the existing 12.38% in the above table, the 7.64% ITC cost of total capital would become 8.08%:

Component	Share of Cap. Structure	Return per above	Weighted Return
LT Debt	70.30%	5.63%	3.96%
Equity	29.70%	13.88%	4.12%
Cost of Total Capital			8.08%

However, cognizant that this Commission regulates its rates and has granted incentives in the form of heightened returns on equity, ITC Holdings has arranged its internal finances such that its operating subsidiaries have artificially equity-heavy capital structures, in the range of 60% equity, 40% debt. That is an unusually thick equity ratio. By way of comparison, the average common equity ratio among ITC's eight Midwest utility proxies is 51.9%, according to

[78] In their Iowa testimony (Exh. CPN-1, Schedule B, page 4 of 6, lines 27-29) Applicants project a roughly 10.558% rate of return on total capital, comprising a 13.88% return on an applied 60% equity ratio, and a 5.575% return on an applied 40% long-term debt ratio.

ITC's witness.[79] By investing the proceeds of ITC Holdings debt as "equity" in its subsidiaries, ITC Holdings doubles the dollar value of return on equity heighteners. Through the present application, ITC seeks to achieve[80] an ITC Midwest total return that is far more lucrative than either of the prior two tables:

Component	Share of Cap. Structure	Return per above	Weighted Return
LT Debt	40.00%	5.63%	2.25%
Equity	60.00%	13.88%	8.33%
Return on Total Capital			10.58%

Of course, notwithstanding these financial manipulations, holders of ITC Holdings' common equity gain ITC's consolidated residual profit, and ITC's consolidated cost of debt is the actual consolidated interest rate paid to bondholders. Consequently, the effective rate of return on equity capital, given a 13.88% ROE applied to a nominal 60/40 capital structure, would be an astonishing 22.3%. That is, after subtracting the 3.96% actual weighted cost of debt from the 10.58% weighted return on capital shown above, the effective weighted return on equity would be 6.62%. Dividing by the 29.70% actual equity ratio, **the effective unweighted rate of return on equity would be 22.30%!**

But all of this financial jiggering serves no apparent ratepayer purpose. It is not even clear that ITC Midwest will issue substantial debt of its own, much less evidence that such issuance would prudently serve ratepayer purposes. Most of the consolidated ITC debt is that of ITC Holdings, the parent, and Wall Street analyses look to this consolidated debt.

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[79] See Exh. IT-4, Schedule 5, page 2.

[80] As cited in note 78 above, Applicants have projected a slightly lower long-term debt rate, 5.575%, which when combined with their proposed predominantly-equity capital structure would yield 2.2 basis points less in return on total capital (10.558% rather than 10.58%). This difference is both small and uncertain, since the proposed formula rate would flow through whatever the actual identified-to-ITC-Midwest debt cost turned out to be.

Accordingly, to the extent it approves any above-cost return on equity, the Commission should apply that inflation only to the 30% share of ITC's capital structure that genuinely represents outside investor equity.

At most, only a 50% imputed equity ratio should apply. ITC Witness Lesser asserts that although ITC Midwest's proposed 60% common equity ratio is well above the proxy group average, it "falls within the range of the proxy group firms" because MDU and Otter Tail have even higher equity ratios. Exh. IT-4 at 66. But MDU and Otter Tail differ strikingly both from the other proxies and from ITC in the percentage of total company revenues that derive from regulated operations. Based on Exh. IT-4, Schedule 5, page 1, this regulated/total revenue percentage was 100% for ITC, 85.8% for the six proxies other than MDU and Otter Tail,[81] and 77% for all eight proxies taken together — but only 22% and 28% for MDU and Otter Tail respectively.

As Value Line notes, much of MDU's revenues are from "oil & gas production, aggregates mining, construction materials production" and much of Otter Tail's revenues are from "manufacturing, plastics, health services, & others," including "Idaho Pacific, which processes dehydrated potatoes" and therefore faces such risks as the current "shortage of raw potatoes."[82] Obviously, MDU and Otter Tail are carrying extra equity so that the operating risks of their non-regulated operations are offset by the reduced financial risks associated with carrying a higher percentage of common equity in their capital structures. The fact that these outliers have slightly more than 60% equity in their capital structures does not make a 60%

[81] This calculation sums total and regulated revenues (as shown at Exh. IT-4, Schedule 5, page 1) across the six firms and then calculates their ratio. Averaging the regulated/total percentages for these six proxies on a per-capita basis returns a similar result, 84.8%.

[82] See the February 9, 2007 Value Line for MDU and the December 29, 2006 Value Line for Otter Tail.

equity capital structure appropriate for a firm, like ITC, that derives all of its revenues from regulated operations. *A fortiori* (and with apologies to McDonald's), if ITC is allowed supersized returns, those returns should not be applied to a capital structure that is rationalized only by comparison with one designed to cover, literally, risks associated with French fries.

For the other six firms, the common equity ratios shown in the last column of Exh. IT-4, Schedule 5 average out to 48.5%. Rounding up to 50% yields the same common equity ratio that is used for rate purposes in MISO's American Transmission Company zone. This is the highest reasonable ratio if ITC Midwest is viewed (incorrectly) as financially distinct from ITC Holdings.

4. Other Components of the "Total Incentive Package" Sought by ITC Heighten the Excessiveness of a 13.88% Return on 60% Equity

The Commission has made clear that even if a proposed ROE falls within the zone of reasonableness and would apply to investment that is eligible for incentives, the Commission will consider the "total incentive package," and will ensure that it is not overly festooned with ribbons and bows. *See* Order 679-A, P 6 (emphasis added):

> The Final Rule stated that the nexus test is to be applied separately to each incentive, rather than to the package of incentives as a whole. We agree that this approach fails to protect consumers where an applicant both seeks incentives that reduce the risk of the project and seeks an enhanced rate of return on equity (ROE) for increased risk. We will therefore grant in part rehearing and require applicants to demonstrate that the total package of incentives is tailored to address the demonstrable risks or challenges faced by the applicant .... If some of the incentives in the package reduce the risks of the project, that fact will be taken into account in any request for an enhanced ROE.

Here, the financial "risks and challenges" faced by ITC Midwest would be vanishingly small. To the contrary, over-recovery would be assured by the proposed zeroing out of IPL's

ADIT balance, the requested formula modification described by ITC Witness Neff, the proposed us of an inappropriate year-end rate base with no administrative necessity to do so, and ITC's proposed unique Appendix I relationship with MISO.

a) ADIT

In years past, IPL paid substantially less in taxes than it collected from ratepayers for tax coverage, because actual taxes paid were reduced by accelerated depreciation, while ratepayers made "normalized" payments for tax coverage that deferred recognition of the tax effects of this depreciation. This same acceleration is why the "tax basis" net book value of IPL's facilities is now significantly less than the "regulatory" net book value. But this tax savings represented an advance to the company from ratepayers (again, they funded IPL's tax payments before IPL actually paid them), not investment by shareholders. Accordingly, under the longstanding rate policy[83] that is embodied in the MISO Attachment O rate formula, the accumulated total of the associated deferred income taxes — Accumulated Deferred Income Tax, or "ADIT" — has been recorded in Accounts 255, 282, and 283, and deducted from the rate base on which IPL earns a return.

Of particular significance, IPL has a large balance in Account No. 282, "Accumulated Deferred Income Taxes — Other [other than accelerated amortization] Property." According to its FERC Form 1 for 2006, this Account No. 282 balance exceeds $410 million. IPL FERC Form 1 at 113, filed May 1, 2007. With the transaction, ratepayers would lose the ADIT deduction that they have earned by pre-paying their share of IPL's income tax liability. On the

[83] *See Pub. Sys. v. FERC*, 709 F.2d 73, 83 (D.C. Cir. 1983) (reciting and relying on "the Commission's policy of deducting accumulated deferred taxes from the rate base. The Commission reasons that a utility should not earn a return on funds contributed by ratepayers."); *Memphis Light, Gas & Water Div. v. FERC*, 707 F.2d 565, 568 (D.C. Cir. 1983) (stating that "because the deferred account is composed of monies contributed by ratepayers and is available to the utility for investment without finance charges, the amount of funds included in the account is

ITC Midwest books, according to ITC's proposed Journal Entries, nothing would be booked to Account 282 or any other regulatory liability account. *See* Exh. N-2. Similarly, for IPL, proposed Journal Entry No. 9 would move $75 million out of Account 282, so that it would no longer be deducted from rate base. *See* Exhibit _____ (CAH-1), Schedule G, page 1 of 3.

As Mr. Linxwiler explains (*see* Affidavit), this ADIT disappearance would increase the zone's annual transmission revenue requirement by almost $12 million. This estimate is based on the roughly 10.558% rate of return on total capital projected by Applicants (*i.e.*, 13.88% return on 60% equity, and 5.575% return on 40% long-term debt):

$74,797,343 rate base increase
* 10.558% return on capital
* (1+49.28% consolidated income tax factor)
= $ 11,788,796.

In a zone with a total ATRR of about $77 million (under IPL), that is a major piece of the rate picture. The rate base would be greatly, but artificially, enlarged, through an accounting adjustment, without any increase to actual transmission assets.

Of course, from a tax standpoint, the premium above the regulatory book value that is being paid to IPL shareholders will result in stepping up the tax basis of the facilities being transferred, to the actual price paid by ITC — a price in line with the artificially increased revenues that result if ADIT is no longer deducted from rate base. But that standpoint is irrelevant, because ratemaking, in a distinction that has long been (and continues to be) followed to ratepayers' detriment, looks to the subsidiary's imputed "stand alone" liability for taxes on return on regulatory book value, not to flow-through of the parent's taxation of gain on tax book value.

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deducted from the rate base. In this way, the ratepayers need not pay the utility a rate of return on their own

The only reason IPL has an ADIT account in the first place is its election to maintain two sets of books, one for tax purposes and one for rate purposes, in order to defer the rate recognition of the tax savings from accelerated depreciation. Consequently, ratepayers paid for IPL's taxes before IPL actually had to pay them, and whether or not any actual payment was ever made. ITC is proposing to maintain this tax/regulatory distinction, by requiring ratepayers to continue paying "an allowance for income taxes," whether or not ITC actually pays them. Consequently, ratepayers will be required to pay a hefty tax allowance, through the MISO Attachment O gross-up formula, without regard for the fact that ITC will be able to significantly reduce its income tax liability, through multiple loopholes. (For example, ITC Holdings has substantial income tax loss carryforwards to apply against any actual income tax exposure.[84]) ITC even proposes to amplify this tax/regulatory distinction by calculating the gross-up tax allowance to reflect the inflated return on equity associated with the artificially thickened 60% equity ratio of ITC Midwest, rather than reflecting the fact that ITC Holdings has proportionately smaller income taxes because it has a much more leveraged capital structure and applies its proportionately larger debt interest expense as an offset against taxable income. In short, the tax accounting cannot reasonably drive this aspect of ratemaking.

Even from the irrelevant standpoint of tax accounting, IPL will not bear full taxation of the income associated with the full difference between the former tax book value and the $750

money.").

[84] Presumably, the ITC group will pay taxes only at the holding company level, and treat ITC Midwest as a pass-through non-taxable LLC, as *ITC*Transmission has been treated. At the ITC Holdings level, potential tax liabilities will be substantially mitigated by the parent's substantial tax loss carry-forward. *See* ITC's October 4, 2006 Prospectus at F-29 ("We have federal income tax operating loss carryforwards of $68.1 million as of December 31, 2005, all of which we expect to use prior to their expiration in 2023 and 2024.").

million price, because the "transco tax incentive"[85] will allow eight years of deferrals in recognizing that gain in taxes.[86] Since the deferred taxes do not accrue interest (whereas the cash received by IPL does grow through investment returns), this deferral significantly reduces the discounted present value of the tax liability associated with the gain on sale.

We recognize that when ITC*Transmission* was spun off, the Commission approved a more limited ADIT write-off to cover the difference between the pre-divestiture regulatory book and the pre-divestiture tax book values.[87] We also recognize that when METC was formed through a pre-settled transaction, the Commission allowed METC to eliminate a considerably smaller ADIT balance. In doing so, the Commission expressly relied on the facts that "Applicants have avoided costly litigation … by entering into stipulations with the affected transmission-dependent utilities and state commission and that these entities support the transaction," and approved the proposed ADIT treatment based on "the fact that the proposal is uncontested." *Trans-Elect, Inc.*, 98 F.E.R.C. ¶ 61,368 at 62,590-91 (2002). But neither case controls here, because ITC Midwest has neither limited itself to avoiding taxation on the difference between regulatory and tax net book nor made the significant concessions that METC gave to secure customer and state commission support.

The proposed massive write-off of ADIT should be disallowed. Even if it is allowed, it must be considered in the weighing of the "total package" of requested incentives. Eliminating the significant ADIT regulatory liability would further ease the mild risks and challenges of owning IPL's monopoly transmission facilities, and significantly sweeten its upside.

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[85] Internal Revenue Code, 26 U.S.C. § 451(i), as extended by Section 1305 of Energy Policy Act of 2005 (EPAct 2005), Pub. L. No. 109-58, 119 Stat. 594 (2005).

[86] *See, e.g.*, Exh. N-3, page 2, Proposed Journal Entry No. 16.

[87] *Int'l Transmission Co.*, 92 F.E.R.C. ¶ 61,276 (2000).

b) Formula Modification and Rate Aspects of Appendix I Modification

During what IPL now confesses was a period of little transmission investment, IPL has been enjoying the benefits of MISO's standard "lagging" rate formula. Under that formula, the prior year's year-end costs are divided by the prior year's 12 CP loads (*e.g.*, year-end 2006 costs divided by the 2006 12 CP), to derive a unit rate that is then applied to monthly CP billing determinants during the succeeding June-through-May service year (*e.g.*, to monthly CP network load during June 2007 through May 2008). While not unfavorable to TOs in a period of stagnant or declining net investment per unit of load, this regimen does have some volumetric risk (and that risk is already reflected in the DCF results for the MISO TO proxy group).

Now that ITC envisions increased annual investment, however, it wishes to switch the formula rate regimen to a current one, with a true-up procedure, such that effectively, unit rates as trued up will reflect the current calendar year's year-end costs divided by the current calendar year's load. This proposed new regimen eliminates volumetric risk. With it, the trued-up bills will divide the current year's revenue requirement by the current year's 12 CP and bill the resulting unit rate to the current year's monthly peak loads. *See* Exh. IT-2 at 6-7. This approach will exactly collect the current year's year-end revenue requirement, with interest to the extent that the true-up mechanism defers its collection, and with zero risk of under-recovery — indeed, with assurance of over-recovery, because year-end costs will be divided by year-long load, producing an assured mismatch that will over-recover costs, as the Commission has recognized both long ago and recently.[88]

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[88] *See, e.g.,* Deficiency Letter issued by the Office of Energy Markets and Reliability in *Baltimore Gas and Electric Co.,* Docket No. ER07-576-000 on May 4, 2007, at 2 & n.2 (questioning use of year-end balances, noting that "Commission policy requires an average of 13 monthly balances for transmission-related balances, including CWIP," and citing *San Diego Gas & Electric*, 118 F.E.R.C. ¶ 61,073 at P 29 (2007)); *ComEd*, 119 F.E.R.C. ¶ 61,238, P 80 (setting for hearing "the formula's use of end of year values for prepaid expenses and materials and

The only risk remaining is the nominal, *de minimis* risk is that a MISO customer would fail to pay its bill. That risk is not material here, for multiple reasons. First, each MISO customer has to provide ample payment security pursuant to Attachment L of MISO's tariff. Second, the predominant customer using what would become ITC's facilities would be IPL, which is a fully credit-worthy entity, and will become even more so (if that is possible) upon receiving the proposed hefty above-book premium for its transmission assets. Third, even if a default somehow did occur, MISO has in place uplift procedures under which ITC's revenue requirement would continue to be paid. Fourth, under the uniquely expansive Appendix I language being proposed by ITC, ITC would have the right to design rates, terms, and conditions for the use of its facilities, and therefore would have enhanced Section 205 filing rights to protect itself in the unforeseeable circumstance of MISO failing to fund ITC's approved revenue requirement. *See* Part III.D above.

Given these multiple protections, it is simply not possible for the many entities that serve load in the wide MISO region to avoid contracting to use MISO's grid. It therefore is not credible to believe that the Commission-approved revenue requirement for ITC Midwest transmission facilities will not be collected by MISO and remitted to ITC Midwest.

In short, even on top of the excessive 13.88% return on an inflated 60% equity share of investment, the filing's other rate-related proposals, concerning ADIT, the Attachment O rate

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supplies in rate base"); *Lockhart Power Co.*, 4 F.E.R.C. ¶ 61,337, at 61,802 (1978) (reversing as contrary to Commission policy an Initial Decision that had approved use of a year-end rate base); *Florida Power & Light Co.*, 56 F.P.C. 3581, 3633 (1974) ("The contentions of the Company to the contrary notwithstanding, the important principle enunciated by the Commission which requires sales volumes, revenues and expenses to be adjusted whenever the use of a year-end rate base is sought cannot be ignored. FP&L has made no such adjustments and it has not shown by any detailed evidence, as contrasted with bare allegations, why and how that principle of synchronization is not applicable here."); *Nevada Power Co.*, 56 F.P.C. 84, 86 (1976); *New England Power Co.*, 9 F.E.R.C. ¶ 63,056 (1979) ("The average plant balance for a test-year should reflect the balance at the beginning and end of the year and all months in between. In this way, rate base is properly matched with revenues received and expenses incurred between the first and last day of the test year."); *Public Serv. Co. of Ind.* 56 F.P.C. 3003, 3025 (1976).

formula, and Appendix I, are also highly and unjustly favorable to Applicants. They wipe out a substantial regulatory liability, accelerate ITC's cost recovery, inflate it by applying a year-end rate base, and render it immune to volumetric and other risks. These changes reduce the proposed transaction's risk and enhance its upside. They must be considered part of the "total package" of incentives at issue, and as such they further militate against allowing a 13.88% ROE or 10.58% return on total capital.

B. Effect on Regulation

The Municipal Coalition has concerns about the impact of this transaction on state regulation. However, recognizing that the Commission's policy is not to consider such impacts where a state commission has authority to consider the transaction,[89] the Municipal Coalition is raising those concerns in state proceedings rather than here.

C. Effect on Competition

Applicants repeatedly assert that the Transaction will promote competition because of the improvements that ITC Midwest will make to the grid as an independent Transco, with no affiliations with any market participant. *See, e.g.*, Application at 16. However, provisions in the Asset Sales Agreement ("ASA"), the Distribution-Transmission Interconnection Agreement ("DTIA") and the Transition Services Agreement ("TSA") create a situation where IPL will be a favored customer, undermining the claimed positive impact on competition unless modified.

DTIA §§ 7.1/7.5: Applicants[90] hail Section 7.1 of the DTIA, which imposes on ITC Midwest a "public utility duty to operate, maintain, plan and construct the Transmission System so that the system is adequate: (a)(i) to support effective competition in energy markets without

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[89] *See* Order 642 at 31,914.

[90] *See* Application at 54 & n.106, quoting DTIA § 7.1(a).

favoring any market participant; (ii) to deliver on a reliable basis the reasonable, projected needs of all loads on the electric distribution systems connected to and dependent upon [ITC Midwest's] facilities for delivery of reliable, low-cost and competitively priced electricity to such distribution systems; and (iii) to provide needed support to the distribution systems interconnected to the Transmission System." DTIA § 7.1(b) requires ITC Midwest to treat IPL's distribution system needs and loads in a non-discriminatory manner, and not to directly assign charges unless approved by the appropriate regulatory body. DTIA § 7.5 further commits ITC Midwest to plan and construct new interconnections to meet IPL's load growth and reliability needs, and to recover costs in accordance with DTIA § 7.1(b) (*i.e.*, to roll-in those costs unless their direct assignment is authorized), but this commitment is apparently not subject to the DTIA §7.1(b) non-discrimination obligation.

These provisions grant IPL the sole right to enforce crucial public utility obligations, and thus are a recipe for undue preference by ITC Midwest in favor of IPL, and undue discrimination against all other loads and generators in the ITC Midwest area. DTIA § 27.3 makes clear that "Nothing in this Agreement, express or implied, is intended to confer on any person other than the Parties hereto any rights, interests, obligations or remedies hereunder."[91] While the DTIA § 7.1(b) non-discrimination provision places some limits on the actions IPL can require under DTIA § 7.1 (but not with regard to interconnections ITC Midwest must construct to meet IPL's needs under DTIA § 7.5), no other transmission customer can contractually enforce such public utility obligations against ITC Midwest. While the FPA of course has its own non-discrimination provisions, these contractual provisions may invite the difficult-to-detect undue

[91] In data responses in the Iowa proceeding pertaining to ASA § 7.13 (discussed below), Applicants confirmed that the provision barring third party beneficiaries means that only IPL could enforce the contractual provision. See IPL's response to Municipal Coalition Data Request No. 2.15, Attachment 8 hereto ("Other transmission customers

preferences that independent transcos were intended to avoid. At minimum, to avoid an adverse impact on competition, the DTIA must be revised to eliminate the no-third–party-beneficiary provision, so other customers can hold ITC accountable contractually in the same manner as IPL, *e.g.*, through DTIA § 21.5 (right to compel performance) and DTIA § 21.4 ("take whatever action at law or equity as may be permitted under this Agreement").

ASA § 7.13(b): Under this provision, ITC Midwest could withdraw from MISO during the first five years after closing with, but only with, IPL consent. Like the no-third-party-beneficiaries provision discussed above, this provision gives ITC Midwest reasons to prefer IPL's views as to RTO participation, while not according the same deference to the views of state commissions or embedded network customers. It also encourages ITC Midwest to favor IPL when and as necessary to secure IPL's consent. This provision should not be left as an IPL-only veto on ITC's RTO affiliation choice. Instead, ITC Midwest should be required to stay in MISO for at least five years unless <u>all</u> MISO customers serving load in the ITC Midwest area consent to an early withdrawal.

TSA § 1(f)/Confidential Schedule C: Under this section of the TSA, right after the closing IPL will supply a capital project schedule to ITC Midwest and ITC Midwest agrees to implement the capital projects set forth in the schedule. There appears to be no requirement restricting the capital project schedule to the projects to which IPL has already committed or Confidential Schedule C, the IPL-identified projects that ITC Midwest has already reviewed and agreed to pursue.

No other transmission customer gets its wires needs comparably "wired in." Conspicuously absent is any effort to engage with other customers as to whether the projects on

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'in the ITC Midwest area' are not third party beneficiaries of the Asset Sale Agreement.").

Confidential Schedule C or the TSA capital project schedule are the most efficient and effective way to address the many pressing problems with the IPL grid. Nor are other customers asked to identify areas of greatest concern, through, *e.g.*, a joint planning process. ITC has not even committed to duplicate in Iowa the "Partners in Business" quarterly meeting process that it practices in Michigan, which at least provides regular updates on ITC planning and construction and an opportunity for stakeholder dialogue with ITC senior management. Nor is there any mention of coordinating with MISO with regard to the IPL-demanded upgrades.

None of this evidences the independent grid management for which ITC Midwest seeks to be so richly compensated. Rather, it seems very much like the "same old, same old," with IPL extending its preferential influence over planning and expansion of the ITC Midwest facilities.

The Municipal Coalition's concerns with regard to the Confidential Schedule C and the IPL capital project schedule under the TSA are not theoretical. To the contrary, our review of Confidential Schedule C reveals projects designed to benefit IPL needs, without including the fixes needed to make the grid serve the needs of neighboring customers. For instance, consider the possible project identified in the third bullet on page 29 of Confidential Schedule C.[92] Municipal Coalition member Missouri River Energy Services is involved (along with Alliant, Great River Energy, and the Midwest ISO) in the Worthington Load Serving Study pertaining to Southern Minnesota, which is supposed to be completed by August. That study could identify the need for a different solution that would render the third-bullet project unnecessary. This third-bullet project is one about which MRES staff happens to have relevant knowledge. That knowledge does not give us comfort that other projects identified in Confidential Schedule C reflect sufficient study on IPL's or ITC Midwest's part to ensure that they are well-selected --

[92] Applicants' FERC-filed Confidential Schedule C eliminates the numbering contained copy of that document filed

i.e., the projects that ought to be selected from the public interest perspective of efficiently and effectively benefiting all customers that rely on IPL's facilities.

More generally, Confidential Schedule C fails to address deficiencies in IPL's system that directly impact service to Municipal Coalition members. Review of the Confidential Schedule C by Municipal Coalition transmission planners reveals that the vast majority of the identified changes to the IPL's capital budget are directed toward projects likely to produce retail load-serving benefits for IPL, with little or no benefits to other transmission customers. Without revealing the contents of Confidential Schedule C or CEII, it appears that only a small fraction of the increased capital expenditures is earmarked toward accelerating or adding projects that might begin to address some of the congestion and access issues affecting Municipal Coalition members.

Thus, Mr. Schultz's testimony (Exhibit No. IT-3 at 22) that "ITC has concluded that the projects are prudent and should be constructed for the benefit of IPL customers" apparently means just that—for the benefit of IPL retail and wholesale power customers, rather than the MISO transmission customers dependent on the IPL transmission system. While Confidential Schedule C would not be surprising from a vertically integrated transmission owner that uses its control over transmission expansion to benefit itself, it hardly appears consistent with the independent, non-discriminatory planning and expansion that ITC claims it will provide. Nor has any effort been made by ITC to solicit information from Municipal Coalition members as to what transmission projects are needed and should be given priority.

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in Iowa as Confidential Schedule H. Page 29 is the third to last page.

In short, Applicants cannot claim that ITC Midwest's independent grid management will enhance competition when they propose and contractually commit to IPL-directed planning and expansion schedules.

D. Consistency with the Public Interest, As Reflected by Commission Policy

A significant portion of the Application is directed toward demonstrating that the transaction is consistent with the public interest, defined by Commission policy. The Applicants argue that the transaction is needed to enable ITC Midwest to make the investments IPL is unwilling to make in the IPL grid. Applicants' testimony details the results of IPL's apparent neglect. According to IPL witness Larsen (Exh. IP-1at 8, lines 5-6 and at 11 lines 2-3), IPL has been unwilling to invest in the grid even where doing so would lower IPL's own energy costs. ITC witness Schultz describes how constraints on IPL's system have resulted in designation of a new MISO Narrow Constrained Area (Exh. IT-3 at 20-21), and how ITC Midwest would construct the projects identified by IPL planners, but not planned to build, and more. *Id.* at 21-22. In testimony before the Iowa Commission, IPL witness Collins graphically describes IPL management as rejecting planning department system proposals to accelerate the replacement of facilities:[93]

> One area of concern is 500 miles of 34.5/69kV lines were constructed prior to 1940. That means those facilities are at least 67 years old. In addition, IPL's 115kV system in central Iowa has been identified as being in poor condition and needs to be rebuilt. There are over 300 miles of 115 kV line in that area.

[93] Direct Testimony of Douglas C. Collins before the Iowa Utilities Board, Docket No. SPU-07-110, at 37, filed March 30, 2007 (excerpt attached hereto as Attachment 9). (References in Mr. Collins' Iowa testimony of Confidential Schedule H correspond to Confidential Schedule C filed by Applicants with this Commission.)

He also describes Confidential Schedule C as "additions the IPL's Planning Department recognizes as necessary," which would be built "over a longer time frame than optimal," while relying on "operating guides" in the meantime.[94]

And what does IPL get for its neglect? It hits the jackpot. It gets rewarded by a $350 million acquisition premium, almost twice the book value of its transmission facilities (1.7709 multiplier, per the Asset Sales Agreement ("ASA") definitions). ITC then asks this Commission to accept ITC Midwest's proposed rates to make payment of this exorbitant acquisition premium rational, even though Commission policy forbids direct recovery of such a premium. *See* Welch Direct Testimony at 8, Exh. IT-1.

So what will vertically-integrated utilities learn if the Commission accepts this transaction as proposed? That rich rewards for stockholders are in store if they follow IPL's lead by starving the transmission system. Phrased another way, the lesson amounts to powerful incentives *not* to embrace the spirit, much less the letter, of the planning and expansion directives included in Order 890.[95] The Municipal Coalition appreciates that transcos, particularly inclusive transcos that accommodate public power participation and tether their rates to costs,

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[94] *Id.* at 37-38. Witness Schultz cites this Schedule as "Schedule H," using its Iowa lettering.

[95] Preventing Undue Discrimination and Preferences in Transmission Service, Order No. 890, 72 Fed. Reg. 12,226 (Mar. 15, 2007), III F.E.R.C. Stat. & Regs. ¶ 31,241 (to be codified at 18 C.F.R. pts 35 and 37) *compliance deadlines extended,* 72 Fed. Reg. 19,112 (Apr. 17, 2007), 119 F.E.R.C. ¶ 61,037 (2007). *See, e.g.*, P 59 ("Expansion of the transmission system, as well as more efficient use of the grid, will alleviate the growth of congestion in most regions of the country"); P 61 ("The decline in transmission investment and increase in transmission congestion underscore our concerns over inadequate planning provisions of the existing pro forma OATT.... With inadequate levels of investment in the grid and increasing transmission congestion, customers' ability to access alternatives to the transmission provider's resources is limited.); P 435 ("New section 217 of the FPA further supports reform in this area, as it reflects Congress' intent that the Commission utilize its powers to facilitate the planning and expansion of the transmission system"); P 927 (describing the Final Rule as emphasizing transmission expansion); *see also* FPA § 217(b)(4), 16 U.S.C 824q ("The Commission shall exercise the authority of the Commission under [the FPA] in a manner that facilitates the planning and expansion of transmission facilities to meet the reasonable needs of load-serving entities to satisfy the service obligations of the load-serving entities, and enables load-serving entities to secure firm transmission rights (or equivalent tradable or financial rights) on a long term basis for long term power supply arrangements made, or planned, to meet such needs").

can play a beneficial role in enhancing the transmission infrastructure on which they depend. But it would be inconsistent with the public interest to approve transco formation in a manner that tells vertically integrated utilities that they are better off evading than embracing Order 890 planning and expansion obligations.

Thus, in assessing the proposed transaction, the Commission must make sure that it does not undermine the planning and expansion policies it is working so hard to implement.

III. THE COMMISSION SHOULD SUMMARILY REJECT OR MODIFY APPLICANTS' SECTION 205 FILINGS, SUSPEND ANY ACCEPTED RATE FOR THE MAXIMUM FIVE MONTHS, AND AT MINIMUM GRANT A FULL EVIDENTIARY HEARING

Part II above shows that the Applicants' core FPA Section 205 rate increase proposals, and thus the Section 203 application that turns on them, should not be accepted as filed. In Part III.A below, we summarize our recommended disposition of those proposals. We then turn to other aspects of the Section 205 filing. Part III.B addresses the cost support information that ITC should be directed to provide annually to customers and state officials as auditable support for its formula rate updates, consistent with Commission precedent. Part III.C addresses the changes the Commission should require with regard to the DTIA and the TSA.. Finally, Part III.D identifies significant flaws in the "Appendix I" through which ITC seeks to structure its relationship with the Midwest ISO.

A. Rates

As demonstrated above, there is no substantial evidentiary basis for increasing the Midwest ISO's rates in what is presently called the Alliant West zone. To the contrary, based on Applicants' own testimony with a few clearly necessary corrections, the just and reasonable cost-based rate would apply a return on equity of 8.74% (median) or at most 9.36% (midpoint).

The Commission should rule summarily that no rate increase has been supported. Absent such ruling, the Commission should find that the proposed rate increase may be substantially excessive — *i.e.*, that 10% or more (in fact, 100%) of the proposed rate increase has not been shown to be just and reasonable — and accordingly should impose a maximum, five month suspension under *West Texas*,[96] starting no earlier than 60 days after Applicants' June 5, 2007 amendment. And it should set any unrejected rate increase for full, trial-type evidentiary hearing, with the discovery rights and time that are essential to due process.

The Commission should also find that Applicants have failed to satisfy the prerequisites for above-cost incentive rates under Order 679. Most important, they have not shown — to the contrary, their evidence shows the opposite — that the proposed rates are within the zone of reasonableness. See Part II.A above. Furthermore, because the Midwest ISO will operate the facilities at issue both before and after the proposed disposition, the only hunting ground for a public interest benefit that could justify an above-cost incentive is the prospect that ITC may eventually undertake beneficial new investment, and in so doing target useful rather than merely rate-base-increasing development. Even if one takes a leap of faith and assumes that that will occur, there is no adequate nexus between incenting such <u>new</u> investment and increasing the return associated with <u>existing</u> facilities. To the contrary, as discussed above, funding an acquisition premium by increasing the return on existing facilities will encourage other transmission owners to follow Alliant's example and let their transmission systems degrade.

Finally, given Applicants' evasive treatment of the effect of its transaction on transmission rates (described in Part II.A above), Applicants should be held to their repeated representations that until January 1, 2009, transmission rates will not change from IPL's

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[96] *West Texas Utils. Co.*, 18 F.E.R.C. ¶ 61,189, 61,374 (1982).

Appendix O rates that become effective June 1, 2007, with no fine print providing for those rates to change through true-up (with interest) to ITC's actual 2008 revenue requirement (including the excessive equity return and ADIT adjustment), threatening severe rate shock (which Applicants make no effort to estimate) in 2010, when imposed in conjunction with ITC Midwest's projected 2010 revenue requirement.

B. Rate Basis Information Requirements

ITC Midwest should be directed to comply with the information requirements that were recently ordered for its METC affiliate, in *Michigan Electric Transmission Co., LLC,* 117 F.E.R.C. ¶ 61,314 (2006), *clarified,* 118 F.E.R.C. ¶ 61,139 (2007). The Commission directed that both customers and the relevant state commission be provided the information needed to "evaluate the accuracy of projected costs that form the basis of Michigan [E]lectric's rates," 118 F.E.R.C. ¶ 61,139 at P 13. This requirement should also apply to the actual costs that will form the basis of ITC Midwest's trued-up rates. *See TrAIL* at P 59 (directing "a detailed accounting of all costs based upon 'company records,'" and itemized true-ups of estimated and actual costs); *cf. ComEd* at P 80 (setting for hearing "formula rate protocols for interested parties to challenge annual updates").

C. Jurisdictional Contracts

Applicants seek Commission acceptance of the Transition Services Agreement ("TSA") and the Distribution-Transmission Interconnection Agreement ("DTIA"). As discussed in Part II.C. above, provisions of these agreements have not been shown to be just, reasonable and not unduly discriminatory and should be modified.

- **DTIA §§ 7.1/7.5** grant IPL the sole right to enforce crucial public utility obligations, and thus are a recipe for undue preference by ITC Midwest in favor of IPL. While the DTIA § 7.1(b) non-discrimination provision places some limits on the actions IPL can require under DTIA § 7.1 (but not with regard to interconnections ITC Midwest must construct to meet IPL's needs under DTIA § 7.5), Section 27.3 bars other transmission customer from enforcing the contractual public utility obligations against ITC Midwest. To avoid creating an incentive and opportunity for difficult-to-detect preferences, the DTIA must be revised to eliminate the no-third–party-beneficiary provision, so other customers can hold ITC accountable contractually in the same manner as IPL.

- **Section 1(f) of the TSA**, an agreement that can last up to three years, provides that after closing IPL will supply a capital project schedule to ITC Midwest and ITC Midwest agrees to implement the capital projects set forth in the schedule. No other transmission customer gets to direct ITC Midwest's transmission upgrades in this manner. Nor are these upgrades assured to be the same as those identified in Confidential Schedule C, which itself is a product of a bilateral discussions between ITC and IPL and, as discussed above, may not effectively and efficiently address known problems, much less provide the promised non-discriminatory service for customers other than IPL. Nor is MISO given any role with regard to evaluating these upgrades. To be just, reasonable, and not unduly discriminatory, and ensure that the upgrades are not limited to those focused on the needs of IPL to the exclusion of other transmission customers, the TSA should be modified to provide that the upgrades should be a product of a coordinated, open and transparent process (which can take place *before* closing) for planning and prioritizing the needed upgrades.

D. ITC Midwest's Appendix I

ITC Midwest states, with respect to its proposed Appendix I to the MISO OATT, that "[t]he provisions contained in this Agreement are derived substantially from the *pro forma*

Midwest ISO Appendix I and from comparable agreements and tariff provisions previously approved by the Commission, including the ITC*Transmission* Appendix I Agreement." Application at 52. Contrary to this assertion, however, provisions of ITC Midwest's proposed Appendix I depart dramatically from the MISO *pro forma* Appendix I ("*pro forma* Appendix I") and from what the Commission has approved in the past, even as to ITC*Transmission*. Indeed, it appears that the Commission has yet to approve portions of the ITC*Transmission* Appendix I, and those portions cannot be relied upon in support of ITC Midwest's proposed Appendix I.

ITC*Transmission* filed its proposed Appendix I on August 31, 2001,[97] and re-filed it with a "Supplemental Agreement" on November 15, 2001.[98] *Int'l Transmission Co.*, Docket Nos. ER01-3000-000, ER01-3000-001, RT01-101-000, RT01-101-001. The Commission accepted the ITC*Transmission* Appendix on December 20, 2001 in *International Transmission Co.*, 97 F.E.R.C. ¶ 61,328 (2001) ("*ITCTransmission*") but declined to act on several provisions at that time because ITC*Transmission* was still a wholly-owned subsidiary of DTE Energy Company, and the Commission believed that it would be more appropriate to act on certain provisions when ITC became independent of market participants.[99]

ITC has referred to the ITC*Transmission* Appendix I as having been approved in *ITCTransmission*. *See, e.g.*, International Transmission Company Motion for Leave to Answer and Answer, filed December 7, 2005 in *Midwest Independent Transmission Systems Operator, Inc.*, Docket No. ER02-2458-000, at 1 n.1. It does not appear that the Commission has made any determinations with respect to the ITC*Transmission* Appendix I since *ITCTransmission* issued

[97] *Available at* eLibrary accession no. 20010910-0275.

[98] *Available at* eLibrary accession no. 20011210-0026.

[99] "[W]e will make final determinations on the designated Special Provisions after the occurrence of the Independence Event." *ITCTransmission* at 62,542.

on December 20, 2001, nor that ITC has requested such Commission action. Several issues with respect to ITC*Transmission*'s Appendix I have therefore not been resolved. Where the Commission declined to decide an issue in *ITCTransmission*, we so state.

To ensure consistency with Commission policy and protect ratepayers, ITC Midwest's Appendix I should be revised.[100]

1. Rates, terms and conditions

a) Setting rates, terms, and conditions

Section 4.2 of the ITC Midwest Appendix I states that "ITC Midwest shall have the right to establish tariff rates, terms and conditions of service under the Midwest ISO Tariff for transactions within the ITC Midwest Zone." There are apparently no constraints on the exercise of that right (beyond Commission review). There is no corresponding provision in the MISO *pro forma* Appendix I. Placing ITC Midwest's rates, terms, and conditions of service "under the Midwest ISO Tariff" does not save this provision from flaws that the Commission rejected in *TRANSLink Transmission Company*, 99 F.E.R.C. ¶ 61,106 (2002) ("*TRANSLink I*"), *on reh'g*, 101 F.E.R.C. ¶ 61,140 and *Alliance Companies*, 99 F.E.R.C. ¶ 61,105, 61,437 (2002) ("*Alliance*").[101]

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[100] ITC Midwest's Appendix I states that ITC Midwest is a signatory to the Midwest ISO Transmission Owner Agreement, whose terms are incorporated except in the event of conflict. ITC Midwest fits within the definition of Owner under the MISO TO Agreement. *See* Article I, Section J. Were it not for the fact that the MISO Transmission Owners Agreement includes, *inter alia*, a provision holding customers harmless in the event that an Owner withdraws from MISO and a provision imposing an obligation to construct consistent with the MISO Plan, the Municipal Coalition would raise such concerns here. If ITC Midwest believes that it is not an Owner for purposes of the Transmission Owners Agreement, it should so state, so the Commission and stakeholders can assess what additional protections are required in Appendix I.

[101] On the same day that it issued *ITCTransmission* partially accepting the ITC*Transmission* Appendix I, the Commission directed the Alliance Companies, which had been attempting to form an RTO, to instead explore options for joining MISO. *Alliance Co.*, 97 F.E.R.C. ¶ 61,327 (2001). *Alliance*, issued April 25, 2002, addressed the Alliance Companies' efforts to comply with that requirement as an ITC.

Specifically, the Commission has previously refused to allow independent transmission companies to set the rates, terms, and conditions of transactions within MISO. In *TRANSLink I*, the Commission allowed TRANSLink to file its revenue requirement and incentive rates—not rates, terms, and conditions—only for transactions with both source and sink in the TRANSLink footprint, and only after consultation with MISO. *TRANSLink I* at 61,455, 61,464-65; see also *Alliance* at 61,435.

Further, in refusing to allow TRANSLink to maintain its own tariff, the Commission stated that "[i]t is important for the RTO to operate under a single tariff with only necessary variations from zone to zone. Multiple tariffs unnecessarily undermine the unity of the RTO region." *TRANSLink I* at 61,464. Furthermore, while TRANSLink was allowed to maintain a separate schedule within the MISO Tariff, the Commission cautioned that "[i]n designing a separate schedule to be included in the Midwest ISO tariff, TRANSLink must minimize... differences." *Id.* If ITC Midwest is allowed to unilaterally set the rates, terms and conditions for service within its zone without regard for whether variations from the MISO Tariff are necessary, the unity of the MISO RTO region will be undermined even if the ITC Midwest variations are nominally "under" the Midwest ISO Tariff.

Section 11.3.1 of the ITC*Transmission* Appendix I provided that "Customers scheduling transactions which have both a point of receipt (source) and point of delivery (sink) within the International Zone shall have the option of purchasing transmission service under the MISO OATT or the International OATT, as applicable."[102] Significantly, however, the Commission

[102] It is noteworthy that the ITC Midwest provision, which would grant it authority to establish rates, terms and conditions "for transactions within the ITC Midwest Zone" may go beyond ITC*Transmission*'s, which would apply only to transactions that both source and sink within the ITC Midwest Zone.

declined to act on that provision due to ITC*Transmission*'s non-independent status, *ITCTransmission* at 62,550.

ITC Midwest's authority over rates, terms and conditions should be restricted consistent with *TRANSLink I*.

b) Rate Pancaking

ITC Midwest's Appendix I, unlike the MISO *pro forma* Appendix I (at Section 3.3), does not contain a provision barring rate pancaking. Non-pancaked rates are a key pro-competitive attribute of an RTO, which ITC Midwest should not be allowed to defeat. Order 2000.[103] The Commission should require that the Applicants add to the ITC Midwest Appendix I a provision identical to Section 3.3 of the *pro forma* Appendix I.

2. Planning

ITC Midwest's Appendix I places insufficient obligations on ITC Midwest to maintain and upgrade its transmission system in a cost-effective manner.

a) Ultimate responsibility for planning

Section 6.1 of the ITC Midwest Appendix I authorizes ITC Midwest to make its own plan, which will then be included in MISO's plan. The ITC Midwest Appendix I states that "Midwest ISO approval is *not* required for the ITC Midwest plan (subject to any dispute resolution), which shall become part of the Midwest ISO regional plan." ITC Midwest Appendix I § 6.1 (emphasis added). In contrast, Section 10 of MISO's *pro forma* Appendix I expressly

[103] Regional Transmission Organizations, Order No. 2000, 65 Fed. Reg. 809, 915 (Jan. 6, 2000) [1996-2000 Regs. Preambles] F.E.R.C. State & Regs. ¶ 31,089, 31,173 ("As described in the NOPR, the elimination of rate pancaking for large regions is a central goal of the Commission's RTO policy."), *order on reh'g*. Order No. 2000-A, 65 Fed. Reg. 12,088 (Mar. 8, 2000), [1996-2000 Regs. Preambles] F.E.R.C. Stat. & Regs. ¶ 31,092, *appeal dismissed for want of standing sub nom. Pub. Util. Dist. No. 1 v. FERC*, 272 F.3d 607 (D.C. Cir. 2001).

provides for dispute resolution as to whether an independent transmission company's plan may be incorporated into the MISO plan, as well as any MISO disagreement with the ITC plan:[104]

> 10.1 ...Midwest ISO approval is not required for the ITC plan, subject to any dispute resolution as provided in Section 10.2 of this Appendix. Such ITC plan shall become part of the Midwest ISO regional plan, subject to Section 10.2.
>
> 10.2 ... If the Midwest ISO disagrees with the ITC's plan, the Midwest ISO's disagreement with the plan will be resolved through dispute resolution.

The failure of ITC Midwest to clearly address disagreement between MISO and ITC Midwest regarding ITC Midwest's plan and/or inclusion of ITC Midwest's plan in the MISO plan could severely undermine MISO's ability to develop an efficient and effective plan for its region, as Order 2000 intends. For example, left to its own devices, ITC Midwest has economic incentives to favor "wires" over "non-wires" solutions. The Commission recognized in *Avista Corp.*, 95 F.E.R.C. ¶ 61,114, 61,341 (2001), *reh'g granted in part*, 96 F.E.R.C. ¶ 61,058 (2001), *clarified*, 96 F.E.R.C. ¶ 61,265 (2001), that this bias may lead to over-building; it found that allowing an independent transmission company to plan expansion subject to RTO veto only if they "impair reliability or Total Transfer Capability" "could result in transmission expansion that, although not inconsistent with reliability, may not treat transmission (wires) and non-wires ... solutions objectively and neutrally if [the RTO] does not consider least cost planning in its approval process." As described above, however, ITC Midwest's Appendix I goes a long way

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[104] ITC*Transmission*'s Appendix I provided that ITC*Transmission* would plan "in coordination with MISO consistent with the provisions and protocols provided for in Appendix B to the MISO [Transmission Owners] Agreement, to the same extent as if International were an Owner for purposes of such Appendix B." § 8.1. Section 8.2, in conjunction with Section 4 of the Supplemental Agreement, gave ITC *Transmission* the option of requesting FERC to grant it greater authority than allowed under Appendix B once ITC became independent. In 2001, as now, Appendix B to the TOA provided for MISO to plan in consultation with representatives of Owners. Section 6 of the Supplemental Agreement subjected disputes related to the ITC*Transmission* Appendix I to "the same dispute resolution procedures as are set forth in Appendix D to the MISO [Transmission Owners] Agreement." The Commission declined to act on Section 8.2 in the absence of more detail. *ITCTransmission* at 62,554.

toward carving its plans out of Midwest ISO's planning process and any "least cost" discipline that process might supply. As the Commission explained in *ITCTransmission* (at 62,554), it is important that any proposal to share transmission planning authority be detailed enough for the Commission to determine "how non-wires solutions will be considered in the decisionmaking process."

The Commission has more recently found even the MISO *pro forma* Appendix I provisions for dispute resolution regarding planning to be insufficient to ensure MISO's responsibility for planning. In *TRANSLink I*, in response to the filing of a draft Appendix I containing language identical to Section 10 of the *pro forma* Appendix I, including the dispute resolution provision,[105] the Commission stated that it

> believe[s] that the RTO, not an outside arbitrator, must have the ultimate authority regarding planning and expansion for its region. Therefore we will require TRANSLink and the Midwest ISO to modify the joint planning protocol such that the Midwest ISO has the final word on planning and expansion that may materially affect facilities outside of TRANSLink which are located within the Midwest ISO.

TRANSLink I at 61,472. In *Alliance*, the Commission rejected another similar proposal:[106]

> Petitioners propose that Alliance GridCo be responsible for planning and expansion of its own system and that the Midwest ISO be responsible for coordinating Alliance GridCo's regional transmission plan. However, we believe that the Midwest ISO, as the RTO, should have the responsibility to ensure that planning and expansion is coordinated across the entire RTO.

Alliance at 61,439.

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[105] *See* Attachment A to Memorandum of Understanding between TRANSLink Parties and MISO, § 10, filed as Exhibit CJM-102 to testimony of Clair J. Moeller, Sept. 28, 2001, in Docket Nos. EC01-156 and ER01-3154 (accession no. 20011003-0384).

[106] *See* Petition for Declaratory Order of the Alliance Companies and National Grid USA, Exhibit B, Section 4.9, filed March 6, 2002, Docket No. EL02-65 (accession no. 20020307-0106).

The Commission should require the Applicants to revise the ITC Midwest Appendix I to clearly give MISO ultimate responsibility for planning throughout the MISO region. At a minimum, the Commission should require the reinsertion of the *pro forma* Appendix I provision for dispute resolution as to whether ITC Midwest's plan is incorporated into the MISO regional plan.

b) ITC Midwest should be required to include all projects in the MISO transmission expansion planning process so that it can qualify to the greatest extent possible for cost sharing

Section 6.1 of ITC Midwest's Appendix I provides that

> [p]rojects included in any ITC Midwest plan shall only qualify for cost allocation under the Midwest ISO Regional Expansion Criteria and Benefits Filings (Attachment FF) through which costs would be sought to be recovered from Pricing Zones outside the ITC Midwest Zone, if the projects have been included in the Midwest ISO transmission expansion planning process.

While this provision is presumably intended as an incentive to participate in the MISO transmission expansion planning process,[107] it may not have the desired effect because ITC Midwest has little interest in whether its upgrades qualify for MISO regional cost allocation. As proposed, ITC Midwest can do its own plan with assured revenue recovery (with excessive returns) through its zonal rate. Unlike vertically integrated TOs, ITC Midwest is not accountable to state commissions (or transmission customers in its zone) as to the level of its transmission rates. Because it has no incentive to keep its zonal transmission rates low, ITC Midwest may not be motivated to seek broader cost allocation. ITC Midwest may well prefer the autonomy afforded under its proposed Appendix I to develop its own plans (described above), rather than subject itself fully to the MISO transmission expansion planning process.

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[107] The cost-spreading mechanism referred to was developed too recently to be reflected in the MISO *pro forma* Appendix I. *See* TEMT Attachment FF § III.

For ITC Midwest to absent itself and its projects from the MISO transmission expansion provision would have adverse consequences for the effectiveness of MISO's planning process. It would also unduly burden ratepayers in the ITC Midwest zone with full cost responsibility for projects whose cost would be eligible for regional or subregional sharing as reliability or regionally beneficial projects.[108] Either through requiring revisions to Appendix I or as a condition of the transfer, the Commission should require ITC Midwest to participate in the MISO transmission expansion planning process for all projects potentially eligible for cost allocation beyond the ITC Midwest zone to ensure cost spreading to the maximum extent.

c) Joint Planning

Furthermore, consistent with Order 890, the Commission should modify Appendix I or take other action to clarify that the ITC Midwest Plan is subject to the joint planning requirement that applies to Transmission Owners in an RTO under Attachment K to the *pro forma* OATT. Particularly given ITC Midwest's proposed independence from the MISO planning process, application of Order No. 890's joint planning requirement is crucial to enhance accountability. Order No. 890 at P 440.

3. Losses

ITC Midwest's proposed Appendix I would allow it to file its own mechanism for determining responsibility for energy losses. Section 3.1. In accepting a nearly identical proposal in 2002, the Commission made clear that the proposal was only a temporary fix:

> As a long-term process, there should be a single method and a single system used to determine losses for the Midwest ISO region

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[108] *See* Regional Expansion Criteria and Benefits Cost Allocation Policy Filings of the Midwest ISO, Docket No. ER06-18, filed Oct. 7, 2005 ("RECB I"), and Nov. 1, 2006 ("RECB II"); Errata to RECB II filed Nov. 8, 2006 in Docket No. ER06-18; *Midwest Indep. Transmission Sys. Operator, Inc.*, 114 F.E.R.C. ¶ 61,106 (2006) reh'g denied, 117 F.E.R.C. ¶ 61,241 (2006); *Midwest Indep. Transmission Sys. Operator, Inc.*, 117 F.E.R.C. ¶ 61,241 (2006); *Midwest Indep. Transmission Sys. Operator, Inc.*, 118 F.E.R.C. ¶ 61,209 (2007).

> so as to preclude to [sic] the potential for creating seams between Alliance and other regions in the Midwest ISO.
>
> On an interim basis, however, we will allow the proposed procedure for calculating losses subject to Petitioner's systems meeting criteria as developed and determined by the Midwest ISO.

Alliance at 61,440. While it might have been appropriate for an Independent Transmission Company to determine losses within its footprint in 2002, there is no reason, five years later, not to rely on MISO's procedure, especially given MISO's determination of losses through its energy market as a component of LMPs, with a refund mechanism for excess marginal loss collections.

4. Most-Favored-Nations Clause

Section 1.3 of the ITC Midwest Appendix I is overbroad and inconsistent with Commission precedent. Section 1.3 states that:

> [I]n the event that, subsequent to the date hereof, Midwest 1SO enters into any agreement or arrangement with or with respect to any current or future Midwest ISO Member or any other ITC, User or transmission customer containing any term with respect to the cost or provision of, or liability for, services which are identical or substantially similar in nature to those being provided under or as contemplated by this Agreement, which term is more favorable to such Midwest ISO Member or ITC, User or customer (a "Superior Term") than any comparable term contained herein is to ITC Midwest or any Relevant Customer (as the case may be), at the option of ITC Midwest and subject to FERC approval, if required, this Agreement shall be deemed amended, on and as of the later of the effectiveness of such Superior Term or any required FERC approval, to the extent necessary or appropriate to incorporate such Superior Term herein in lieu of any such comparable term so that such Superior Term thereafter governs the cost or provision of, or liability for (as the case may be) services under or as contemplated by this Agreement and the relationship of Midwest ISO and ITC Midwest (for itself and with respect to Relevant Customers) under this Agreement.

No party objected to ITC*Transmission*'s similar proposed provision in 2001, and the Commission did not remark on it. However, two years later, the Commission refused to allow

TRANSLink to include an almost identical most favored nations clause in its Appendix I, finding that it would impose an undue administrative burden and create contract uncertainty. *TRANSLink Dev. Co.*, 102 F.E.R.C. ¶ 61,033, P 25 (2003). *See also Ameren Servs. Co.*, 101 F.E.R.C. ¶ 61,320, P 177-78 (2002), *clarified*, 103 F.E.R.C. ¶ 61,178 (2003), *reh'g denied*, 104 F.E.R.C. 61,096 (2003). The burden and risk of contract uncertainty are no less now than they were in 2003; the Commission should reject this provision, as it has done before.

IV. CONCLUSION

For the reasons presented above and in the attachments hereto, the transaction should be rejected, and if not rejected, should be conditioned or modified as follows:

- The formula rate as proposed by Applicants should be modified such that its end result is kept within an empirically supported zone of reasonableness, with
  - the rate of return on equity set no higher than the currently-applicable last clean rate of 12.38%;
  - the capital structure for use in rates made reflective of the highly leveraged capital structure of ITC Holdings; and
  - The ADIT balance, through which ratepayers have pre-funded the payment of income taxes imputed to transmission income, carried forward as an ADIT balance on ITC Midwest's books, and if not carried forward then counted as incentive enough, obviating any above-cost rate of return on capital;
- The rates, terms, and conditions of the Section 205 rate filing, including its Appendix I, should be suspended until 60 days plus five months after the filing was completed, which did not occur before June 5, 2007;
- A full trial-type evidentiary hearing, with discovery rights, should be convened; and
- The remedies discussed above regarding Schedule C, and Appendix I, and the other aspects of Applicants' filing, should be ordered, or at least considered at hearing.

Respectfully submitted,

/s/ Cynthia S. Bogorad

Cynthia S. Bogorad
David E. Pomper
Rebecca J. Baldwin

Attorneys for
Midwest Municipal Transmission Group,
Missouri River Energy Services and
Wisconsin Public Power Inc.

Law Offices of:
Spiegel & McDiarmid
1333 New Hampshire Avenue, NW
Washington, DC 20036
(202) 879-4000

June 20, 2007

CERTIFICATE OF SERVICE

I hereby certify that I have on this 20th day of June, 2007, caused the foregoing document to be sent by first-class or electronic mail to all parties on the list compiled by the Secretary of the Commission in this proceeding.

/s/ Rebecca J. Baldwin

Rebecca J. Baldwin

Law Offices of:
Spiegel & McDiarmid
1333 New Hampshire Avenue, NW
Washington, DC 20036
(202) 879-4000