agreements pursuant to our ratemaking authority under sections 4 and 5 of the NGA and sections 205 and 206 of the FPA, we do not find it necessary to do so in light of the requirement that traditional, centralized service companies (i.e., service companies that are not special-purpose companies such as a fuel supply company or a construction company) file relevant cost-allocation information on FERC Form No. 60. FERC Form No. 60 is a less burdensome method for collecting this information from service companies. Furthermore, where appropriate, we will rely on our ratemaking authority to examine these agreements or require them to be filed on an as-needed basis to determine whether the regulated utility's purchases of non-power goods and services were prudently incurred and just and reasonable.

152. We agree with the numerous commenters who express a desire to protect captive customers from inflated affiliate transactions. However, imposing a blanket requirement to file each cost-allocation agreement for non-power goods and services is not necessary to fulfill our jurisdictional responsibilities. Instead, we believe that the review of cost-allocation information contained in FERC Form No. 60 submissions by traditional, centralized service companies, review of service agreements and other information in the context of rate proceedings, and/or review of cost information through the audit function provide sufficient protection for customers.

b. Inclusion of Natural Gas Companies under Section 1275(b)

153. In the NOPR, we also noted that section 1275(b) provides that holding companies and state commissions may under certain circumstances require Commission review and authorization of cost allocations for non-power goods or services provided by service

companies to public utilities, but it does not provide for such determinations where such non-power goods and services are provided to gas utility companies and natural gas companies. We invited comments as to whether the Commission should recommend an amendment clarifying that holding company systems and state commissions having jurisdiction over gas utility companies and natural gas companies in the holding company systems are included within the scope of section 1275(b).

Comments

154. Commenters were generally supportive of the Commission's proposal in this regard. Dominion and EEI state that such a clarification would be appropriate with respect to holding companies with combined electric utility company and gas utility company systems because cost allocations in those systems will affect both types of companies and the inclusion of both in section 1275(b) would help ensure that a consistent approach is applied throughout the system.[147] NARUC also supports the proposal, arguing that, since gas utility companies and natural gas companies are included in most of the other provisions of PUHCA 2005, their omission from section 1275(b) impacts the Commission's ability to prevent the cross-subsidization of affiliates of public utilities and natural gas companies, as well as effectively eliminating the prior review of the allocation of service company costs upon the request of state commissions

[147] Dominion Comments at 19-20, EEI Comments at 26. See also Ameren Comments at 16, Cinergy Comments at 24-25, Energy East Comments at 12, Keyspan Comments at 5, NASUCA Comments at 3, Northeast Utilities Comments at 6, Oklahoma Corporation Commission Comments at 5.

and holding company systems to public utilities.[148] In addition, NARUC recommends that gas-related agreements be filed with the Commission and that the Commission institute procedures for periodic audits, as discussed above in reference to the electric context.[149]

155. Duke opposes the inclusion of natural gas companies under section 1275(b) because, unlike public utilities, natural gas companies are not subject to the ratemaking authority of state regulatory commissions, and therefore are not in danger of incurring trapped or otherwise unrecoverable costs as a result of conflicting state commission decisions.[150]

Commission Determination

156. In the report to Congress mandated by section 1272(2) of EPAct 2005, we intend to request that Congress clarify whether it intended section 1275(b) to include natural gas companies and, if so, to adopt a conforming amendment. As EEI and Dominion note, many holding company systems include both electric and natural gas companies, utilities, affiliates, and subsidiaries. Maintaining a consistent standard would add to transparency and reduce confusion.

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[148] NARUC Comments at 9-10. See also IURC Comments at 9-10, Ohio PUC Comments at 3-4.

[149] Id. at 10.

[150] Duke Comments at 5. See also NiSource Comments at 9.

c. Adoption of the SEC "At Cost" Standard

157. The SEC and state commissions previously have been primarily responsible for determining allocations of costs for non-power goods and services among the various associate companies in registered holding company systems, and these allocations have been made on an "at cost" basis. By contrast, the Commission's long-standing policy is that registered holding company special-purpose subsidiaries must provide non-power goods and services to a public utility regulated by the Commission at a price no higher than market. For at least a decade, we have imposed this standard as a condition for approval of mergers that result in the creation of a new registered holding company.[151] We invited comments as to whether the Commission should apply the market standard for the allocation of costs for non-power goods and services, or if we should instead adopt the SEC at cost standard.

Comments

158. The comments as to whether the Commission should adopt the SEC's "at cost" standard were mixed, with a number of entities expressing general support for a lower of

[151] See Inquiry Concerning the Commission's Merger Policy Under the Federal Power Act: Policy Statement, Order No. 592, 61 FR 68595 (Dec. 18, 1996), FERC Stats. & Regs., Regulations Preambles July 1996-December 2000 ¶ 31,044 at 30,124-25 (1996) (Merger Policy Statement), reconsideration denied, Order No. 592-A, 62 FR 33341 (June 19, 1997), 79 FERC ¶ 61,321 (1997). Where the regulated public utility has provided non-power goods or services to the non-regulated affiliate, our policy has been that the public utility provides the goods or services at the higher of cost or market.

cost or market standard.[152] APPA/NRECA argue that, first, with respect to purchases of goods and services by the public utility from a non-utility affiliate, a public utility should not pay to a non-utility affiliate a price exceeding what the public utility would have incurred had the public utility self-provided the service or purchased it prudently from an unaffiliated third party; similarly, if the affiliate can produce the good or service at a below-market price, presumably so can the public utility. APPA/NRECA assert that the pricing rule that supports these principles is the Commission's market standard.[153] Second, with respect to the sale of goods and services by the public utility to the non-utility affiliate, APPA/NRECA contend that the price to the non-utility affiliate should be at no less than cost. According to APPA/NRECA, this rule follows from the public utility's obligation to minimize its revenue requirement, and a standard of no less than cost removes any incentive for a public utility to "over acquire" resources and provide them at a price below cost to a non-utility affiliate.[154] Finally, with respect to public utility provision of financial support to affiliated non-utility ventures, APPA/NRECA

[152] See, e.g., Georgia PSC Comments at 3, NASUCA Comments at 10, Northeast Utilities Comments at 6 (Commission should also apply standard to construction activities), Santa Clara Comments at 10-12, TANC Comments at 10-12.

[153] APPA/NRECA Comments at 9. See also Arkansas PSC Comments at 3, Electricity Consumers Resource Council, et al. (ELCON) Comments at 6, Kentucky Public Service Commission (Kentucky PSC) Comments at 1, Missouri PSC Comments at 11, NASUCA 10.

[154] Id. at 10. See also Arkansas PSC Comments at 3, Missouri PSC Comments at 14, NASUCA Comments at 10.

note that section 12(c) of PUHCA 1935 prohibited a registered holding company from receiving any such benefit from a public utility subsidiary or any other subsidiary and urges the Commission to continue this prohibition.[155]

159. APPA/NRECA note that the argument made for service companies is the efficiency of centralization, but argue that the use of such companies can do damage to auditability. The damage arises from the holding company practice, endorsed by the SEC, of charging service company costs to FERC Account 923—Outside Services. According to APPA/NRECA, what appears on the public utility's books is not detail about each service company cost, but instead a single large charge representing the public utility's allocated share of total service company cost. They further argue that the use of the Commission's "Outside Services" account implies an arm's-length relationship between the buyer of the outside services and the supplier; but in fact the relationship between service company and public utility is not at arm's length. APPA/NRECA contend that the solution for this problem would be for the Commission to require an accounting process that treats the public utility operating company incurring these inter-affiliate costs as if the public utility had incurred the costs directly. The public utility then would post the charges to the appropriate accounts (making sure to segregate the costs passed through by the service company from the public utility's own directly

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[155] Id. at 10-11. See also Missouri PSC Comments at 15-16.

incurred costs), thereby facilitating oversight by the Commission and by outside auditors.[156]

160. NARUC supports a lower of cost or market standard, noting that the NARUC Guidelines state that: "Generally, the price for services, products and the use of assets provided by a non-regulated affiliate to a regulated affiliate should be at the lower of fully allocated cost or prevailing market prices. Under appropriate circumstances, prices could be based on incremental cost, or other pricing mechanisms as determined by the regulator." Although the NARUC Guidelines call for more flexibility than was reflected in the NOPR, NARUC asserts that its position and the Commission's standard for the allocation of costs for non-power goods and services are consistent.[157]

161. In their reply comments, Xcel and Progress Energy submit that there are a number of fallacies to the arguments in favor of the market standard. Xcel states that, first, if the affiliated service company charges for its services at cost, it does not and cannot profit from its activities. Second, the notion that at cost pricing could cause a utility to pay a service company more for services than it would otherwise incur is, as a practical matter, also wrong. Third, the underlying premise of service company formation is that such administrative and general activities can be performed more efficiently and at a less costly rate by a service company on behalf of a utility than a utility could perform the

[156] APPA/NRECA Comments at 29.

[157] NARUC Comments at 20.

service for itself.[158] Progress Energy contends that, typically, service companies provide administrative services such as tax, accounting, human resources, legal, information technology, finance and shareholder relations, which are materially different from other products or services needed by a utility such as fuel, vehicles, poles, transformers, etc. Specifically, the services provided by a service company are not fungible, and there is no market for such specialized services.[159]

162. On the other hand, the majority of commenters favor the continued use of the SEC's at-cost standard. Dominion and EEI argue that the Commission has not demonstrated the need to revise the current standards. They assert that the cost-allocation factors found in registered holding company system service agreements have been worked out in cooperation with both the SEC and the relevant state commissions, and that there is no evidence that the application of this standard has led to cross subsidization or other forms of abuse.[160] MidAmerican emphasizes that public utilities have relied on the at cost standard as the basis for assigning the costs of non-power goods and services and that these costs may be subject to the provisions of an intercompany services agreement which has received state regulatory approval and have proven to work well.[161]

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[158] Xcel Reply Comments at 3-4.

[159] Progress Energy Reply Comments at 2.

[160] Dominion Comments at 17, EEI Comments at 22-23. See also Cinergy Comments at 21-22, Entergy Comments 9, E.ON/LG&E Energy Comments at 14, FirstEnergy Comments at 14, Keyspan Comments at 4, Progress Energy Comments at 3, Southern Company Services Comments at 4.

[161] MidAmerican Comments at 13-14.

In addition, Entergy argues that its existing retail rates are based on the at-cost standard and any changes will disrupt existing agreements and retail rate structures.[162] MBIA Insurance, however, also asserts that many utilities have already committed to using a lower-of-cost or market standard as part of various mergers. It contends that holding companies already applying the lower of-cost-or-market standard for non-power goods and services should continue meeting this requirement and not disrupt pre-existing arrangements.[163]

163. Dominion and EEI further argue that there is no need to revise these standards because the Commission can address this issue in ratemaking proceedings. Given the repeal of PUHCA 1935 and section 318 of the FPA, they assert that there is no longer an impediment to the exercise of the Commission's powers under sections 205 and 206 of the FPA to disallow particular expenditures made at cost that the Commission finds to be imprudent.[164] AEP adds that cost-based standards also have the benefit of being verifiable and easy to audit.[165]

164. EEI further asserts that a market test can be difficult to apply for highly-specialized goods or services because there is no market for the services supplied by a system service company and, thus, it can be extremely difficult to calculate a market

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[162] Entergy Comments at 9. See also Alliant Comments at 5-6, Keyspan Comments at 4, Progress Comments at 4.

[163] MBIA Comments at 17.

[164] Dominion Comments at 18, EEI Comments at 23-24. See also Cinergy Comments at 23, E.ON/LG&E Energy Comments at 14, Xcel Comments at 6.

[165] AEP Comments at 5. See also Cinergy at 23.

price for such services. None of these difficulties accompany the at-cost standard.[166] Similarly, MidAmerican argues that, by using cost, the public utility company or affiliate is not required to undertake a potentially lengthy and subjective process to ascertain what a market price would be for the non-power goods or service, which in many instances, such as the allocation of employee labor, is not readily available due to the variation in pay scales across the industry and the country.[167] Moreover, EEI argues that there is a significant danger of under-recovery of costs under the Commission's market standard where the service company's cost to provide a service is higher than market. Thus, while the at-cost standard keeps the service company whole, a lower of cost or market standard can lead only to under-recovery and an increase in the regulated utilities' cost of capital.[168] Finally, Oklahoma Corporation Commission opposes the adoption of the Commission's market basis because it might impose additional costs on such entities due to potential requirements that companies enter into a competitive bidding processes, hire consultants, enter into special contracts, and use variable pricing structures based on the

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[166] EEI Comments at 23. See also Alliant Energy Corporation (Alliant) Comments at 5-6, Ameren Comments at 16, AEP Comments at 6, Cinergy Comments at 22, Energy East Comments at 13, Entergy Comments at 10, E.ON/LG&E Energy Comments at 14, FirstEnergy Comments at 15, Keyspan Comments at 4, Progress Energy Comments at 4, Southern Company Services Comments at 4, Xcel Comments at 6.

[167] MidAmerican Comments at 13.

[168] EEI Comments at 23. See also Ameren Comments at 15, AEP Comments at 6, Duke Comments at 4, Entergy Comments at 10, Energy East Comments at 13-14, FirstEnergy Comments at 14.

different services that are provided.[169] Santa Clara responds that the at-cost standard allows the holding company to bill its utility affiliate for the total cost of the non-power goods or services, no matter how unnecessarily high the costs might be. Thus, the holding company has no incentive to minimize its costs.[170]

165. Energy East and EPSA contend that the Commission lacks the authority to impose its pricing standard. Energy East asserts that the plain language of section 1275(b) indicates Congress' intent that the Commission should retroactively review costs and then properly allocate them. Nothing in section 1275(b), argues Energy East, indicates that Congress intended that the Commission pre-approve the cost of non-power goods and services rendered to associated public utilities under a lower of cost or market pricing standard.[171] EPSA argues that the Commission does not have authority under the FPA, NGA or PUHCA 2005 to approve the formation and corporate structure of any company in a holding company system, let alone companies that propose to provide services to holding company system companies. Thus, while the Commission has the authority to disallow a utility's recovery in its jurisdictional rates of improper affiliate charges, the Commission does not have the authority to regulate transactions among non-utility affiliates by requiring at-cost pricing, and, therefore, has no authority to impose financial

[169] Oklahoma Corporation Commission Comments at 5-6.

[170] Santa Clara Comments at 12.

[171] Energy East Comments at 12.

and complex accounting and reporting requirements to implement at-cost pricing.[172]

166. Finally, some commenters suggest alternatives to switching to the SEC's at-cost standard. Dominion argues that service companies that have been subject to the SEC at-cost standard under PUHCA 1935 should be permitted to continue using that standard if they so elect.[173] American Transmission Company recommends that the Commission establish a rebuttable presumption that cost equals market for those companies that can demonstrate that they have appropriate purchasing practices in force for those goods or services above a certain dollar amount.[174] Entergy states that the Commission should not preclude holding company systems from deviating from the at-cost standard to the extent that such alternative pricing proposals are demonstrated to not result in inappropriate cross-subsidization of non-utility associate companies.[175] IURC states that, while in most cases, the SEC's fully-distributed cost may be appropriate, there will be instances where the market standard will be appropriate; specifically, where there is reasonable confidence that the market is sufficiently competitive to produce an unbiased competitive price. In the absence of a competitive market to determine the appropriate arm's-length

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[172] EPSA Comments at 10-11.

[173] Dominion Comments at 17, EEI Comments at 22-23. See also Black Hills Comments at 4, Energy East Comments at 13, FirstEnergy Comments at 13, NiSource Comments at 14, Northeast Utilities Comments at 5, Southern Company Services Comments at 4.

[174] American Transmission Company Comments at 4.

[175] Entergy Comments at 10-11.

value for a specific transaction, incremental costs might be appropriate.[176]

Commission Determination

167. As an initial matter, some commenters appear to misconstrue the purposes of the Commission's request for comments on the use of the SEC's "at-cost" standard. Contrary to EPSA's implication that the Commission seeks to approve the formation and corporate structure of companies within a holding company system, this was not the subject of the Commission's proposal or request for comments. Rather, there are two circumstances in which the "at-cost" or "market" standard may arise in the context of the Commission's jurisdictional responsibilities. First, the Commission has a responsibility to ensure that the costs of non-power goods and services provided by a traditional, centralized service company to public utilities within the holding company system are just, reasonable, and not unduly discriminatory or preferential. This can arise in the context of a review of the prudence of costs incurred when a public utility seeks to flow through the costs in jurisdictional rates or a general review of the justness and reasonableness of the public utility's costs. It can arise in the context of an individual public utility within the holding company system or in the context of the appropriate non-discriminatory allocation among multiple public utilities within the same holding company system.[177] In reviewing centralized service company cost allocations, the

[176] IURC Comments at 11.

[177] While the Commission would have authority to require pre-approval of non-power goods and services cost allocations to public utilities that want recovery of such costs in Commission-jurisdictional rates, the Commission historically has not taken such an approach, and instead typically reviews such matters at the time the public utility files

Commission's focus would be on the costs allocated to the jurisdictional public utilities, whether the jurisdictional public utilities are bearing their fair share of costs vis-à-vis the non-regulated affiliates (i.e., whether the non-regulated affiliates are receiving an undue preference), and whether costs are fairly allocated among public utilities. If the Commission disallowed costs to be allocated to public utilities or changed the allocation among multiple public utilities, this would not directly affect allocations to the non-jurisdictional, non-regulated companies. Our concern and jurisdictional responsibilities relate to how the costs are allocated to and among Commission-jurisdictional companies, not how remaining costs are allocated among the non-regulated affiliates.

168. The second context in which the "at-cost" or "market" standard is likely to arise is when a service company that is a special-purpose company within a holding company (e.g., a fuel supply company or construction company), provides non-power goods or services to one or more public utilities in the same holding company system. The same potential issues arise: whether the public utility's costs incurred in purchasing from the affiliate are prudently incurred and just and reasonable, and whether non-regulated affiliates purchasing non-power goods and services from the same special-purpose company are receiving preferential treatment vis-à-vis the public utility. The Commission in this context also, if it found costs were imprudent, unjust and unreasonable, or unduly discriminatory vis-à-vis the public utility, would develop a rate or remedy applicable to the jurisdictional public utility.

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for rate recovery.

169. With these two types of situations in mind – traditional, centralized service companies and service companies that are special-purpose companies – we reach the following conclusions based on the comments. The Commission will not require traditional, centralized service companies currently using the SEC's at-cost standard to comply with the Commission's market standard for their sales of non-fuel, non-power goods and services to regulated affiliates. Fundamentally, we agree with commenters such as American Transmission Company and Progress Energy that centralized provision of accounting, human resources, legal, tax and other such services benefits ratepayers through increased efficiency and economies of scale. Further, we recognize that it is frequently difficult to define the market value of the specialized services provided by centralized service companies. Accordingly, the Commission will apply a rebuttable presumption that costs incurred under "at cost" pricing of such services are reasonable. However, we will entertain complaints that "at cost" pricing for such services exceeds the market price, but complainants will have the burden of demonstrating that that is the case.

170. We also agree with commenters such as Dominion and EEI that the Commission has the power to disallow any expenditures that it finds to be imprudent under sections 205 and 206 of the FPA, and sections 4 and 5 of the NGA. Additionally, the

audit function can be used to identify and protect against any cross-subsidization between regulated public utilities and non-regulated affiliates.

171. With respect to non-power goods and services transactions between holding company affiliates other than traditional, centralized service companies, i.e., service companies that are non-regulated, special-purpose affiliates such as a fuel supply company or a construction company, we will continue our prior policies.[178] First, with respect to sales from a public utility to a non-regulated, affiliated special-purpose company, we agree with APPA/NRECA that the price should be no less than cost, i.e., the higher of cost or market; otherwise, a public utility could attempt to game the system and forego profits it could otherwise obtain by selling to a non-affiliate, to the benefit of its non-regulated affiliate who receives a good or service at a below-market price. When the situation is reversed, i.e., the non-regulated, affiliated special-purpose company is providing non-power goods and services to the public utility affiliate, the Commission will continue to apply its market standard. The non-regulated, affiliated special-purpose company may not sell to its public utility affiliate at a price above the market price. We believe that such transactions involving such non-regulated, affiliated special-purpose

[178] Our adoption of different policies for traditional, centralized service companies compared to special-purpose companies could make the distinction between the two more important than it has been previously. We view the former as performing generally corporate administration functions and the latter as providing generally a single input to utility operations, such as fuel supply, construction, or real estate. If holding companies are unclear about whether a subsidiary is a traditional, centralized service company or a special-purpose company, they may seek a determination in an appropriate proceeding. We will also monitor the issue through the auditing process.

companies pose a greater risk of inappropriate cross-subsidization and adverse effects on jurisdictional rates.

172. APPA/NRECA note that section 12(c) of PUHCA 1935 prohibits a public utility from providing financial support to affiliated non-utility ventures, and they suggest that the Commission continue this prohibition through its regulations. Congress did not reenact this provision of PUHCA 1935 in PUHCA 2005, and, although we believe we have authority under the FPA and NGA to impose such a restriction, we do not believe such a restriction is necessary at this time.

173. We find that APPA/NRECA raise some valid points concerning service company billings and how those amounts should be reflected in the accounts of a public utility company. However, resolution of this issue may have policy implications as well as practical accounting system implementation issues that should be explored more broadly than the record in this proceeding allows. Therefore, we decline to adopt at this time APPA/NRECA's recommendations on this issue.

174. We disagree with Energy East and EPSA that section 1275 of PUHCA 2005 in any way restricts this Commission's authority to impose either the market standard or the at-cost standard. By remaining silent on the standard to be employed, Congress has placed the matter squarely within the Commission's discretion. Contrary to assertions by EPSA and others, the Commission is not exceeding its authority by establishing policies governing the sale or provision of non-power goods and services by a non-regulated company to an affiliated public utility. The standard used affects jurisdictional rates, and the Commission has the authority to establish a standard insofar as it pertains to

jurisdictional rates pursuant to its ratemaking authority under sections 205 and 206 of the FPA and section 4 and 5 of the NGA, as well as pursuant to the additional authority to review and authorize cost allocations requested under section 1275 of EPAct 2005.

d. Other Issues Regarding Cost-Allocation Agreements

Comments

175. APPA/NRECA assert that the language of proposed section 366.5(b) could be misinterpreted to mean that a company "organized specifically" for one purpose (say, providing legal services to the system's utility members) and that later takes on other responsibilities (like providing accounting services to the system's utility members) can escape review under this section (for example, at the request of a state commission). Such "after-acquired" functions should not preclude Commission review.[179] Similarly, MBIA Insurance contends that, even if the non-utility associate exists primarily for another purpose, such as providing services to companies outside of the system, its intra-system costs to regulated utilities should still be subject to the Commission's review, if a state or holding company opts for Commission review. To the extent that the Commission believes it may lack the authority to adopt such a regulation, MBIA Insurance urges the Commission to ask Congress to clarify or grant the Commission this authority to protect customers and prevent regulatory gaps.[180]

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[179] APPA/NRECA Comments at 8. See also Missouri PSC at 9.

[180] MBIA Insurance Comments at 18.

176. A number of commenters expressed concern about the potential preemptive effect of Commission review of cost-allocation agreements. In order to avoid any preemption issue, NARUC suggests that the filing of such agreements occur under section 304 of the FPA and section 10 of the NGA, instead of under section 205 of the FPA and section 4 of the NGA.[181] Missouri PSC states that a Commission-approved allocation should bind Commission ratemaking but not state ratemaking, except in limited circumstances, and urges the Commission to make clear that a state commission is not preempted by any Commission-determined service cost allocation, whether the initiating entity is a holding company system or another state commission.[182] In addition, Missouri PSC urges the Commission not to interpret section 1275(b) to permit gaming of the state commission retail ratemaking process by holding companies or state commissions, i.e., to permit state commissions or holding companies to petition the Commission to review and authorize a holding company system-wide cost-allocation methodology that would be imposed on all state commissions. Finally, Missouri PSC contends that an interpretation of section 1275(b) giving Commission-approved cost allocations preemptive effect would also be contrary to the clear language contained within section 1275(c), which provides that: "Nothing in this section shall affect the authority of the Commission or a state commission under other applicable law." Since state commissions have state law

[181] NARUC Comments at 2.

[182] Missouri PSC Comments at 9.

authority to set retail rates, including authority to disallow purchase costs or sales prices deemed unreasonable or imprudent, section 1275(c) on its face protects the state commissions from any asserted preemptive effect of a Commission allocation under section 1275(b).[183]

177. By contrast, Xcel and NiSource contend that any Commission-approved cost allocations under section 1275 will necessarily preempt state determinations. Xcel argues that it would negate the intent of Congress to give the Commission the authority to review these allocations if state commissions could undertake their own cost allocations and urges the Commission to avoid any kind of actions or statements that would support the argument that the preemptive effect of section 1275 is dependent on the form of filing of service agreements with the Commission.[184] NiSource states that it fails to see how the Commission can approve service company cost allocations that will apply to entities across multiple states if one of these state commissions can then simply refuse to accept the Commission's cost allocation as binding. For this reason, NiSource requests that the Commission needs to provide certainty in the final rule that a Commission-approved cost allocation is binding on the states.[185]

178. Dominion and EEI contend that the primary situation in which the Commission would need to impose a specific methodology would be a situation in which a multi-state

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[183] Id. at 11-12. See also Progress Energy Comments at 9.

[184] Xcel Reply Comments at 5-6.

[185] NiSource Reply Comments at 7.

holding company system finds that all state commissions do not approve a single allocation agreement. In such cases, the multi-state holding company system would apply to the Commission to impose consistent requirements that would eliminate the possibility of trapped costs.[186]

Commission Determination

179. In response to APPA/NRECA's concerns regarding the "organized specifically" language, we clarify that we do not interpret this to allow a cost allocation to escape review if the associate company later takes on additional responsibilities. In response to the comments from MBIA Insurance, the Commission has authority to review any intra-system costs to any jurisdictional company under FPA and NGA authority.

180. In response to the requests for clarification of the potential preemptive effect of section 1264 and the Commission's regulations thereunder, we believe that issues related to preemption are more appropriately addressed on a case-by-case basis to give the Commission the opportunity to consider the potential preemptive effect of section 1264 in specific circumstances. However, we anticipate that such issues would arise only in unusual circumstances.

5. Single-State Holding Company Systems and Other Classes of Transactions

181. Section 1275(d) of EPAct 2005 directs the Commission to issue rules no later than four months after the date of enactment of EPAct 2005 to exempt from the requirements of section 1275 (service allocation requests by holding company systems or state

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[186] Dominion Comments at 18-19, EEI Comments at 25-26.

commission) "any company in a holding company system whose public utility operations are confined substantially to a single state" and any other class of transactions that the Commission finds are not relevant to the jurisdictional rates of a public utility. We interpreted this to exempt single-state holding companies and sought comments on how the Commission should define "confined substantially to a single state."

182. While section 1275(d) states that companies in single-state holding company systems are exempt from the "requirements" of section 1275, section 1275 does not impose any requirements on holding company systems or companies within these systems, but rather grants holding company systems and relevant state commissions the right to obtain Commission review and authorization of cost allocations. Instead, the only requirements in section 1275 are directed toward the Commission, in particular that "the Commission shall review and authorize" cost allocations if asked to do so by the holding company system or the relevant state commission. Based on the structure of section 1275, we suggested that the most reasonable interpretation of the exemption in section 1275(d) is that Congress intended to deny single-state holding company systems and state commissions having jurisdiction over a public utility in such systems the right to obtain Commission review of cost allocations pursuant to section 1275. Accordingly, we proposed to reflect this limitation by excluding single-state holding company systems from the scope of Commission review under section 366.5(b) of the Commission's regulations. The Commission invited comments on this interpretation of section 1275(d).

a. Definition of Single-State Holding Company System Exemption

Comments

183. Some commenters agree with the Commission's interpretation that section 1275(d) exempts single-state holding company systems whose public utilities operations are confined substantially to a single state (i.e., all of the holding companies' public utility affiliates or subsidiaries operate principally in a single state), whereas other commenters (as discussed below) interpret the exemption to apply only to individual "companies" within the holding company system, i.e., where the individual public utility, operating primarily in a single state.

184. A number of commenters who agree with the Commission's interpretation also suggest various modifications to the scope of the single-state holding company exemption and propose definitions of the phrase "confined substantially to a single state." EEI suggests that the Commission follow SEC practice and precedent in interpreting this exemption, in particular, section 3(a)(1) of PUHCA 1935 which provides an exemption for intrastate holding companies. According to EEI, under current SEC practice, a holding company will qualify for the intrastate exemption if it derives no more than approximately 13 percent of its utility revenues from out-of-state public utility company operations. EEI further suggests that, in administering this exemption, the Commission should follow current SEC practice and require the annual submission of information in Part 3 of Form U-3A-2 by companies seeking an exemption under section 1275(d).[187]

[187] EEI Comments at 27-28. See also MidAmerican Comments at 11.

Scottish Power also agrees that Congress intended to deny single-state holding company systems and relevant state commissions the right to obtain Commission review of cost allocations pursuant to section 1275 and urges the Commission to clearly reflect this limitation by excluding single-state holding company systems from the scope of Commission review under section 366.5(b) of the Commission's regulations.[188]

185. NARUC submits that the exemption should apply to any company in a holding company system whose public utility operations are confined substantially to a single state, rather than applying the exemption to the holding company system that is confined substantially to a single state. Thus, the relevant inquiry should involve an analysis of the extent to which the individual company operates in a single state rather than the extent to which the holding company system is predominately single-state in nature.[189] NARUC further asserts that the Commission should follow the SEC's interpretation of this single-state holding company exemption under PUHCA 1935. Consistent with this precedent, NARUC proposes that, if a company in a holding company system whose public utility operation derives 70 percent or more of its gross utility operating revenues from within a single state, that individual company should be considered exempt from section 1275 and any related Commission regulations.[190] NiSource supports the 70 percent threshold

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[188] Scottish Power Comments at 11.

[189] NARUC Comments at 12-13.

[190] Id. See also E.ON/LG&E Energy Comments at 18-19 (the standard should be whether 80 percent or more of the retail customers served by the public utilities in the holding company system are located within a single state).

because, first, it would be unusual for a traditional public utility that has its physical operations in one state to derive more than 30 percent of its gross utility operating revenues from outside that state. Second, NARUC's proposed standard correctly captures the statutory language of section 1275(d); whereas the Commission's proposed language in proposed section 366.5(c) of the NOPR is, at best, ambiguous.[191]

186. Commenters also suggested revisions to the Commission's proposed regulatory text in section 366.5. NiSource notes that the current language can be read so that a holding company with operations in multiple states falls under section 1275(b) even if its public utility is confined substantially (or entirely) to a single state. NiSource urges the Commission to modify the first sentence in section 366.5(c) to read that "any company in a holding company system whose public utility operations are confined substantially to a single state, as defined herein, is exempt from paragraph (b) of this section."[192] Santa Clara and TANC state that, in light of the complexities of effective state oversight and regulations of holding companies, the Commission should interpret the definition of single-state strictly and narrowly to prevent creeping variations from the letter and spirit of the exemption, and avoid a gap in effective regulation of multi-state utility holding company systems. Santa Clara and TANC therefore urge the Commission to reevaluate its interpretation of the single-state holding company exemption from Commission

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[191] NiSource Comments at 9.

[192] Id. NiSource further states that the final rule should make clear that section 1275 applies only to traditional public utilities. In addition, if a traditional public utility engages in wholesale sales beyond its service territory, such sales should not render the utility subject to section 1275.

review under section 1275.[193] Ameren argues that the focus of the term "confined substantially to a single state" should be on the state or states in which a holding company system is subject to retail rate regulation since there are no "captive" customers who could be harmed in a state where the public utility does not have cost-based rates.[194] Finally, Public Citizen contends that the single-state exemption requires that both a public utility and its holding company primarily operate in a single state, so that the state is capable of regulating the holding company, as well as the public utility, under state law.[195]

Commission Determination

187. Despite the ambiguous language of section 1275(d), we believe that the most reasonable interpretation of section 1275(b) and (d) together is that section 1275(b) is designed to offer this Commission as a forum for holding company systems and state commissions to obtain cost allocations within holding companies whose public utility operations are not confined substantially to a single state. Specifically, section 1275(b) is designed to allow multi-state holding companies, or the regulatory agencies of states in which the holding company's public utility subsidiaries operate, to obtain Commission review and authorization of cost allocations. However, Congress in section 1275(d) does not permit single-state holding companies to take advantage of the procedures in

[193] Santa Clara Comments at 14-15, TANC Comments at 14-15.

[194] Ameren Comments at 18.

[195] Public Citizen Comments at 13.

section 1275(b).[196] This means that, if a holding company has several public utility subsidiaries operating in different states, even if the individual subsidiaries' businesses are each confined substantially to a single state, the holding company itself does not confine its public utility operations to a single state, and therefore, the exemption does not apply. On the other hand, if the holding company has multiple non-utility subsidiaries operating in more than one state, but one or more public utility subsidiaries that all operate primarily in the same state, the exemption would apply.

188. Several commenters agree that a holding company should be considered to be a single-state holding company if it complies with current SEC practice on granting a similar exemption under PUHCA 1935, which requires that a certain percentage of public-utility revenues be derived from operations within a single state. We believe it is reasonable to adopt a standard that is consistent with SEC rules and will define a single-state holding company as one that does not derive more than 13 percent of its public-utility revenues from outside a single state.

189. We agree with several commenters that the relevant analysis should be whether a holding company's regulated public utility operations are confined substantially to a single state, not whether the holding company itself is confined substantially to a single state. As discussed above, we interpret the single-state holding company exemption in

[196] With respect to NARUC's alternative interpretation of the scope of this exemption, we note that the phrase "whose public utility operations are confined substantially to a single state" directly follows, and thus modifies, "holding company system" rather than "company." This interpretation is consistent with the structure of section 1275(b) which provides the election to the holding company system, rather than individual companies within it.

section 1275(d) to apply in cases where a holding company has multiple non-utility subsidiaries operating in more than one state, but one public utility subsidiary that operates primarily in a single state. In such a case, the holding companies' public utility operations would be subject to the jurisdiction of a single state commission, while the holding companies' operations would not. Accordingly, we find that Public Citizen's interpretation is inconsistent with the text of section 1275(d).

b. Other Classes of Transactions That Should Be Exempted

190. In the NOPR, we concluded that an exemption under section 1275(d) forecloses Commission review under section 1275(b). In section 366.5(c) of the Commission's regulations, we proposed to establish a procedure by which the Commission, either upon petition for declaratory order or upon its own motion, may exclude from the scope of Commission review and authorization under section 366.5(b) any class of transactions that we determine are not relevant to the jurisdictional rates of a public utility. The Commission invited comments as to other classes of transactions that, pursuant to section 1275(d), should be exempted from the requirements of section 1275.

Comments

191. No comments were received on this subject. Accordingly, we will not at this time establish any blanket exemptions for certain classes of transactions.

6. Previously Authorized Activities

192. Section 1271 of EPAct 2005 states essentially that a person may continue to engage in activities or transactions authorized by rule or order as of the date of enactment of EPAct 2005 if that person continues to comply with the terms of the authorization. In

the NOPR, the Commission proposed to reflect this statutory provision in section 366.6 of the Commission's regulations. The Commission also proposed to require that, if any such activities are challenged in a formal Commission proceeding, the person claiming prior authorization shall be required to provide the full text of any such authorization (whether by rule, order, or letter) and the application(s) or pleading(s) underlying such authorization (whether by rule, order, or letter).

193. A number of commenters have noted that proposed section 366.6 states that persons will be able to continue to engage in activities or transactions authorized under PUHCA 2005, and that it should instead refer to PUHCA 1935. In response to the comments, we have corrected this error in the regulations adopted here.

Comments

194. The majority of the comments supported the Commission's proposal to allow entities to rely on SEC orders, in particular, SEC financing authorizations.[197] For example, Dominion and EEI note that, with the repeal of section 318 of the FPA, many additional public utilities will become subject to Commission jurisdiction under section 204 and that, unless registered holding company public utility subsidiaries can rely on their current SEC orders, it will be necessary for them to apply immediately for Commission authorization under section 204 of the FPA. According to Dominion and EEI, this would create a substantial burden for the holding companies and their public utility subsidiaries and could also lead to a surge in section 204 applications at precisely

[197] See, e.g., Cinergy Comments at 25-27, FirstEnergy Comments at 16-17, National Grid Comments at 7-8, Scottish Power Comments at 12, Xcel Comments at 6.

the time that the Commission is burdened with implementing its new duties under EPAct 2005. Dominion and EEI thus recommend that the Commission in its rulemaking make a finding under section 204 of the FPA authorizing holding company public utility subsidiaries, at their option, to issue securities and assume liabilities following the effective date of PUHCA 2005, provided that they comply with the terms of their SEC financing authorization. Dominion and EEI further recommend that this authorization continue through the later of December 31, 2007 or the date on which the SEC order is set to expire.[198]

195. EEI further suggests that, to the degree it deems necessary, the Commission could condition its acceptance of SEC financing authorizations on specific requirements related to the provisions of FPA section 204, such as the restrictions on secured and unsecured debt set forth in Westar Energy, Inc.[199] However, if the Westar or other conditions are imposed, EEI contends that they should apply prospectively only and not to securities issued prior to February 8, 2006.[200]

196. Entergy supports the Commission's proposed interpretation of the savings provision in section 1271, but asserts that there are several technical concerns regarding the manner in which the proposed rule is drafted that, if not corrected, may prevent the rule from achieving its intended purpose. Entergy urges the Commission to clarify the

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[198] Dominion Comments at 20-21, EEI Comments at 29-30.

[199] 102 FERC ¶ 61,186 (2003), order rescinding authorization, 104 FERC ¶ 61,018 (Westar).

[200] EEI Comments at 30.

condition in the proposed rules insofar as it provides authority to continue to engage in "activities or transactions" approved by the SEC "[u]nless, otherwise provided by Commission rule or order." Entergy inquires if, for example, a Commission section 204 financing order imposes a condition that is not present in an existing SEC financing order issued to another public utility under PUHCA 1935, can the other public utility continue to rely on its PUHCA 1935 order or is the applicability of the saving provision negated by the referenced condition? Similarly, Entergy asserts that there may be a question whether the "unless otherwise provided language" will necessitate compliance with the requirements of Part 34 of the Commission's regulations or other regulatory conditions or requirements adopted by the Commission, to the extent that such requirements are absent from an existing PUHCA 1935 financing order (which otherwise would continue in effect beyond the PUHCA 1935 repeal date as a result of the saving provision).[201]

197. Entergy also seeks clarification as to the statement in the NOPR that existing PUHCA 1935 authorizations are to remain "in effect for the period of time provided in such authorization" with respect to authorizations that do not contain a specified expiration date, in particular, orders authorizing creation of service companies, which typically do not reference any expiration date. Entergy recommends that authorizations granted by the SEC under PUHCA 1935 should remain in effect after repeal, unless and until such time as such authorization would otherwise expire under the applicable PUHCA 1935 order, rule or statutory provision, or until such time as the Commission

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[201] Entergy Comments at 12-13.

issues a new order expressly modifying the authorization previously granted to the applicable company by the SEC under PUHCA 1935.[202]

198. Finally, Entergy requests clarification of the statement in the NOPR that such authorizations will remain effective only "so long as that person continues to comply with the terms of such authorization." According to Entergy, many orders issued by the SEC require periodic reporting to the SEC of financing transactions that are consummated pursuant to the authorization set forth in the order, so the question arises as to whether such reporting requirements will be considered "terms" of the PUHCA 1935 authorization that must be satisfied in order to continue to engage in the SEC-approved financing transactions subsequent to the February 8, 2006. Entergy requests that the Commission clarify that following February 8, 2006, such reports (originally required to be filed with the SEC pursuant to Rule 24, adopted under PUHCA 1935) are to be filed with the Commission, rather than with the SEC.[203]

199. PacifiCorp requests that the Commission clarify that SEC financing authorizations will be preserved for a sufficient period of time to permit a reasonable transition period (through December 31, 2007) to the requirements of section 204 for both utilities and the Commission. PacifiCorp further requests that the Commission provide a mechanism for such further approvals until February 8, 2006, and to preserve tax treatment by retaining

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[202] Id. at 13-14.

[203] Id. See also NiSource Comments at 14-15 (the Commission should clarify that only the SEC's conditions and terms apply, unless the Commission states otherwise in a specific order).

the right of holding companies to avail themselves of Internal Revenue Code section 1081, which section 1271 also preserves.[204]

200. MGTC requests that the Commission clarify that prior status determinations by the SEC remain valid and are grandfathered by the operation of section 1271, so that, for example, if a person was declared not to be a "gas utility company" by the SEC, and the facts on which that determination was made have not materially changed, that person will not be a "natural gas company" under PUHCA 2005 and implementing regulations. MGTC further contends that, if the Commission is not willing at this time to issue a broad declaration that prior SEC status determinations are grandfathered by section 1271, the Commission should nonetheless hold that a person that the SEC found was not a "gas utility company" under PUHCA 1935 will not be required to comply with the Commission's new regulations until the Commission makes an affirmative finding that the person is a "natural gas utility" under PUHCA 2005.[205]

201. Northeast Utilities Service Company (Northeast Utilities) notes that some registered holding companies may have obtained amendments to existing SEC orders or new orders after August 8, 2005, i.e., date of enactment of EPAct 2005, and thus urges the Commission to make clear that such modified and/or new orders should also be grandfathered, if possible.[206]

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[204] PacifiCorp Comments at 7-8.

[205] MGTC Reply Comments at 1, 4. See also Mittal Steel Reply Comments at 2-5.

[206] Northeast Utilities Comments at 6.

202. Some commenters, however, emphasized that section 1271 of EPAct 2005 does not insulate activities previously approved by the SEC from Commission review under the FPA or NGA.[207] According to APPA/NRECA, the savings provision in section 1271(a) of EPAct 2005, which allows entities with SEC approvals to continue engaging in the transactions so approved, does not diminish the Commission's authority to establish conditions that ensure just and reasonable rates under the FPA or NGA.[208] APPA/NRECA further emphasize that any interpretation of section 1271(a) that would limit the Commission's ability to review the effect of particular activities or transactions on Commission-jurisdictional rates would be inconsistent with section 1271(b), which makes clear that section 1271(a) does not circumscribe in any way the Commission's regulatory authority under the FPA and the NGA.[209] Similarly, Santa Clara notes that it might be argued that a conflict between section 1271(a) and 1271(b) arises when SEC rules under PUHCA 1935 require different or less rigorous standards than the Commission's rules under the FPA, e.g. SEC at-cost standard vs. the Commission's market standard. Santa Clara urges the Commission to clarify that all activities, including those previously authorized by the SEC and the Commission itself, are subject

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[207] See, e.g., Arkansas PSC Comments at 7, Missouri PSC Comments at 14-15.

[208] APPA/NRECA Comments at 4. See also Santa Clara Comments at 17, TANC Comments at 17.

[209] Id. at 13-14.

to review, rules, regulations and policy administered independently by the Commission under the FPA.[210]

203. Finally, Oklahoma Corporation Commission suggests that the Commission should amend proposed section 366.6 to include language that clearly articulates that said person or entity should also bear the burden of proof that that person or entity has complied with the rule, order, or letter.[211]

Commission Determination

204. In the NOPR, we noted that the repeal of PUHCA 1935 and section 318 of the FPA would give the Commission jurisdiction under section 204 of the FPA over certain issuances of securities and assumptions of liabilities by companies within holding company systems that are currently subject to the jurisdiction of the SEC. Furthermore, Congress expanded the Commission's jurisdiction over holding company acquisitions of securities through its amendments to section 203 of the FPA in section 1289 of EPAct 2005. Finally, Congress explicitly stated in section 1271(b) that nothing in PUHCA 2005 limits the Commission's authority under the FPA and the NGA. Thus, it is clear that in EPAct 2005 Congress intended to preserve, and in some ways expand, the Commission's authority over issuances of securities, assumptions of liabilities by companies within holding company systems, and holding company acquisitions of securities. However, Congress also included in PUHCA 2005 a transition provision, which allows persons to

[210] Santa Clara Comments at 18-19.

[211] Oklahoma Corporation Commission Comments at 7.

continue to rely on previously-granted SEC authorizations.

205. We will adopt section 366.6 as proposed in the NOPR and allow entities to continue to rely on SEC orders, including SEC financing authorizations. We will also grant a number of the clarifications with respect to SEC financing authorizations requested by commenters. However, the Commission will require all holding companies that intend to rely on their SEC financing authorizations to issue securities, assume liabilities, or engage in securities transactions that would otherwise be reportable under section 203 of the FPA, as amended by EPAct 2005, or section 204 of the FPA to file with the Commission a copy of these SEC orders by the effective date of PUHCA 2005. The filing of these orders will permit the Commission to maintain effective oversight of the previously-authorized activities and transactions that, due to the repeal of PUHCA 1935, are now subject to the Commission's jurisdiction under the FPA.

206. Section 1271(a) states that nothing in PUHCA 2005 or PUHCA 1935 and the rules, regulations, and orders thereunder, prohibits a person from engaging in or continuing to engage in activities or transactions in which it is legally engaged or authorized to engage on the date of enactment of PUHCA 2005, if that person continues to comply with the terms (other than an expiration date or termination date) of any such authorization. This provision, and section 366.6 of our regulations that we adopt herein, permit persons to rely on the SEC multi-year financing authorizations for the period of time provided in that authorization. Accordingly, we clarify that, to the extent companies in a holding company system engage in authorized financing transactions, in compliance with the terms of that authorization, we will not require those entities to seek additional

authorization under sections 203 or 204 at this time.

207. We find that EEI's concerns regarding Westar are beyond the scope of this rulemaking and, therefore, we will not address them here. Instead, the Commission will consider whether to place Westar conditions upon future applications on a case-by-case basis.

208. Section 1271(a) permits a person to engage in previously-authorized activities if that person continues to comply with the terms of that authorization, other than an expiration date or termination date. We agree that it is necessary to provide a reasonable transition period for entities subject to the requirements of PUHCA 2005 and, therefore, we agree with Dominion and EEI that these authorizations should continue through the later of December 31, 2007 or the date on which the SEC order is set to expire and with PacifiCorp that section 204 authorizations should not be required until December 31, 2007, without regard to the duration of the SEC authorization. We conclude that it is reasonable to permit entities to rely on their SEC financing authorizations for the period of their duration or through December 31, 2007, whichever is later. Similarly, with respect to Entergy's request for clarification regarding authorizations for the formation of service companies, which do not have a termination date, we conclude that PUHCA 2005 does not grant the Commission authority over service company formation and thus Commission authorization is not required.

209. We will also grant Entergy's clarification that, after the effective date of PUHCA 2005 (i.e., February 8, 2006), for SEC orders that require periodic reporting to the SEC of financing transactions that are consummated pursuant to the authorization set forth in the

order, such reports are to be filed with the Commission, rather than with the SEC, so long as the company continues to rely on such authorization. We do not think it is reasonable to assume that Congress intended to carry forward the SEC's financing authorizations without the specific reports required to be submitted as a condition of those authorizations. More importantly, the receipt of such reports will allow the Commission to perform its oversight duties, while allowing the entities to continue to rely on these SEC financing authorizations for a reasonable transition period.

210. PacifiCorp appears to be requesting that the Commission grant further financing approvals under PUHCA 1935 until February 8, 2006, since it could not do so under PUHCA 2005, which does not take effect before that date. While the Commission has no authority to take any action under PUHCA 1935, which was entrusted to the SEC, to the extent necessary to permit continuity of financing authorizations or to preserve tax treatment referenced in section 1271(c) of PUHCA 2005,[212] the Commission will entertain requests for financing approvals prior to February 8, 2006, but will be able to make any such approvals effective only upon the effective date of PUHCA 2005, February 8, 2006.

211. As noted, section 1271(c) explicitly states that tax treatment under section 1081 of the Internal Revenue Code of 1986 as a result of transactions ordered in compliance with PUHCA 1935 shall not be affected in any manner due to the repeal of PUHCA 1935 and

[212] Section 1271(c) of PUHCA 2005 states that such tax treatment shall not be affected in any manner due to the repeal of PUHCA 1935 and enactment of PUHCA 2005.

the enactment of PUHCA 2005, and we will comply with this provision insofar as such tax treatment is reflected in jurisdictional rates or in the Commission's Uniform System of Accounts and the SEC's Uniform System of Accounts, as they exist on the day before the date of enactment of PUHCA 2005.

212. We will also grant Northeast Utilities' request that section 1271 will apply to modifications of SEC orders made between the date of enactment and the effective date of PUHCA 2005.

213. We will also grant the clarification requested by APPA/NRECA and others that transactions entered into pursuant to prior SEC authorizations are not insulated from Commission review under the FPA and the NGA. Previously, certain securities transactions were exempted from Commission jurisdiction due to section 318 of the FPA, which Congress has repealed. While we agree that section 1271(a) permits companies within holding company systems to continue to rely on SEC financing authorizations, this authorization simply permits them to engage in such transactions without prior Commission approval under sections 203 and 204 of the FPA, but does not insulate them from our review of jurisdictional rates under sections 205 and 206 of the FPA and sections 4 and 5 of the NGA.

214. We will not adopt Oklahoma Corporation Commission's suggestion that we amend section 366.6 to include language that clearly articulates that said person or entity should also bear the burden of proof that that person or entity has complied with the rule, order, or letter. We find that such an amendment is unnecessary at this time.

7. Exempt Wholesale Generators and Foreign Utility Companies

215. EPAct 2005 repeals PUHCA 1935 in its entirety, including section 32, which requires the Commission to make EWG determinations on a case-by-case basis, upon application. Although the definitional section of PUHCA 2005 references section 32 of PUHCA 1935, the Congress nevertheless repealed section 32 in its entirety and did not re-enact that provision in the new PUHCA 2005. The Commission stated in the NOPR that it believed that the most reasonable interpretation of EPAct 2005, given the omission of section 32 in the new PUHCA 2005, is that Congress did not intend the Commission to continue to make case-by-case determinations of EWG status in the future (i.e., after the effective date of PUHCA 2005). Rather, we stated in the NOPR that the most reasonable interpretation of the statute is that only those entities that are holding companies with respect to persons granted EWG status before the repeal of PUHCA 1935 would qualify for an exemption from the new federal books and records access requirements under proposed section 366.3(a)(2) of the Commission's regulations. Accordingly, we proposed to remove Part 365 of the Commission's regulations, which set forth the filing requirements and ministerial procedures for persons seeking EWG status under section 32 of PUHCA 1935, and we invited comments on whether we should do so.

216. We further noted that the benefit of EWG status under PUHCA 1935 was that entities that the Commission determined to have met the definition of EWG were exempted from the myriad requirements of PUHCA 1935. The principal benefit of being an EWG under PUHCA 2005 is exemption from the new federal books and records access requirements. To the extent that these new federal books and records access

requirements add to the Commission's existing very broad books and records access authority under FPA section 301 and NGA section 8, we concluded that our interpretation served to err on the side of greater customer protection.

217. We also noted that, in any event, entities that qualified as EWGs under PUHCA 1935 were not exempted from the Commission's authority under the FPA if they met the FPA definition of "public utility," including the very broad access to books and records provisions of FPA section 301. Nor will they be exempt from these FPA provisions as a result of PUHCA 2005.

218. In addition, we noted that Congress repealed section 33 of PUHCA 1935, which addresses FUCOs. As with EWGs, we stated our belief that Congress intended to limit the exemption for persons that are holding companies with respect to FUCOs to those attaining FUCO status before repeal of PUHCA 1935. The Commission invited comments as to this interpretation of EPAct 2005.

Comments

219. Some commenters expressed support for the Commission's decision to no longer make determinations of EWG status. These commenters note that, while Congress repealed the section of PUHCA 1935 addressing EWGs, the exemption in subsection 1266(a)(2) refers to these repealed designations, they have to apply to something, and they agree with the Commission's position that the exemptions must apply only to the existing EWGs and FUCOs.[213] Public Citizen agrees that grandfathered EWGs have a

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[213] APPA/NRECA Comments at 21, Georgia PSC Comments at 3, Santa Clara Comments at 18, TANC Comments at 18.

reliance argument for maintaining their status, but disagrees with extending such grandfathering to new entities that are now aware that the distinction no longer exists. Furthermore, Public Citizen states that grandfathered EWGs must continue to comply with EWG requirements to maintain their grandfathered EWG status and that they should be required to make an annual filing with the Commission stating how each continues to comply with the original terms of its EWG or FUCO exemptions.[214]

220. The majority of commenters, however, opposed the Commission's proposal to stop making determinations of EWG status as contrary to Congress' intent and the plain meaning of the statute.[215] According to Calpine, by incorporating the definition of EWG into PUHCA 2005 and relying on that definition to permit holding companies with respect to only EWGs, QFs, and/or FUCOs to be exempt from the federal books and records access requirement, Congress recognized the continuing need for EWG determinations after the repeal of PUHCA 1935 takes effect; nowhere in EPAct 2005 is the exemption limited to holding companies with EWGs prior to the repeal of PUHCA 1935 takes effect. Calpine thus contends that, if Congress wanted to restrict EWG determinations to a certain time period, it knew how to do so, but chose not to.[216] Similarly, Dominion and EEI argue that, by preserving the meaning of the term "exempt

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[214] Public Citizen Comments at 5.

[215] See, e.g., Coral Power/Shell Windenergy Comments at 8, EPSA Comments at 16-17, Goldman Sachs Comments at 5, PPM Energy Comments at 3-4.

[216] Calpine Comments at 5-6 (quoting section 1253(a) of EPAct 2005 defining "existing qualifying cogeneration facility").

wholesale generator" found in PUHCA 1935, Congress in essence preserved section 32(a) of PUHCA 1935, which defines an EWG, in part, as a company that the Commission determines to be an EWG. Thus, according to Dominion and EEI, the Commission's case-by-case determination process is incorporated directly in the definition.[217] Morgan Stanley argues that the Commission's interpretation effectively renders superfluous the EWG exemption contained in EPAct 2005.[218]

221. Other commenters believe that the Commission's interpretation is not a permissible one because the decision to eliminate Part 365 and future EWG determinations would produce unreasonable or unduly discriminatory results. Calpine argues that, under the Commission's interpretation of the statute, if Calpine added one more wholesale generator that would have been an EWG under Part 365, Calpine and its subsidiaries will lose the exemption and thus it is not reasonable for the addition of one wholesale generator that is identical to Calpine's EWG affiliates in every respect but one (i.e., EWG status), to result in all of these companies and their affiliates being subject to the books and records access requirements and SEC rules, particularly when these companies were exempt from regulation under PUHCA 1935 and have no captive customers in need of protection.[219] Further, Calpine asserts that the use of proposed section 366.3(b), which would provide for entities to file for a petition for a declaratory

[217] Dominion Comments at 22-23, EEI Comments at 32.

[218] Morgan Stanley Comments at 7.

[219] Calpine Comments at 6. See also Coral Power/Shell WindEnergy Comments at 8.

order that they are exempt from the Commission's books and records requirements, is not an adequate alternative for Calpine due to the high costs of filing such petitions.[220] Morgan Stanley further argues that comments supporting the Commission's proposed deletion of Part 365 offer no substantive basis for why such a course of action comports with legislative intent, nor do they explain how it will not chill investor confidence or dissuade capital from entering the wholesale generation sector.[221] Finally, Dominion and EEI note that a number of states provide exemptions from state laws based on EWG status and that failure to make additional EWG determinations would also deprive those companies of the benefits of those laws.[222]

222. With respect to determinations of FUCO status, Calpine disagrees with the Commission's proposal in the NOPR. Calpine asserts that, by incorporating the definition of FUCO into PUHCA 2005 and relying on that definition to permit holding companies with respect to only EWGs, QFs, and/or FUCOs to be exempt from the federal books and records access requirement, Congress recognized the continuing need for FUCOs after the repeal of PUHCA 1935 takes effect. As with EWGs, Calpine contends that it is not reasonable for the addition of a single foreign subsidiary having no potential to impact the operations of its domestic affiliates to subject such affiliates to the books

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[220] Id. at 10-11.

[221] Morgan Stanley Reply Comments at 2-3.

[222] Dominion Comments at 23, EEI Comments at 33.

and records access requirement and the SEC rules when they were not subject to such rules under PUHCA 1935.[223]

223. EEI proposes that the Commission should exempt FUCOs from the requirement that they maintain their books and records under proposed Rule 366.2(e), but that they otherwise should be subject to the books and records access provisions of section 366.2 of the Commission's proposed regulations. According to EEI, the Commission should continue to have access to FUCO records to the extent that such records are relevant to the costs incurred by a public utility or natural gas company that is an associate of a holding company and necessary and appropriate for the proper exercise of the Commission's statutory charge under the FPA and NGA with respect to jurisdictional rates.[224]

224. Some commenters suggested that the Commission should adopt a self-certification process similar process to that used by the SEC. For example, Scottish Power argues that FUCOs that operate exclusively outside of the US should not be subject to Commission oversight. The Commission should continue the SEC's practice of allowing for the creation of FUCOs by submittal of a notice filing. FUCOs and their subsidiary operations are generally separate from that of the domestic utility operations and

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[223] Calpine Comments at 8-9. See also EPSA Comments at 16-17, PPM Comments at 3.

[224] EEI Comments at 34. See also National Grid Comments at 5-8. National Grid also argues that extending the Commission's books and records mandates to FUCOs would subject them to conflicting mandates resulting in maintaining separate duplicative books and inappropriately expand the extraterritorial impact of PUHCA 2005 without any benefit to U.S. consumers.

therefore would not bear in any way on the jurisdiction rates of such utility company.[225]

Commission Determination

225. Having again reviewed the ambiguities in statutory construction, and balancing the facts that Congress repealed section 32 of PUHCA 1935 in its entirety, yet referred to section 32 in the definitional sections of PUHCA 2005, we conclude that it is reasonable to interpret PUHCA 2005 to allow entities to obtain EWG status under PUHCA 2005. However, we will reject the requests from various commenters that we retain part 365 of our regulations, which permit only case-by-case applications for EWG status.

226. Instead, in line with the comments received from Scottish Power and others, we will establish a self-certification process for companies that believe they satisfy the criteria for EWG or FUCO status. This process is similar to that used for self-certifications for QFs under the Public Utility Regulatory Policies Act of 1978, and is set forth in section 366.7. Section 366.7(a) provides that the owner or operator of an EWG or FUCO, or its representative, may file with the Commission a notice of self-certification demonstrating that it satisfies the definition of EWG or FUCO. In the case of EWGs, the owner or operator must also file a copy of the notice with the state regulatory authority of each state in which the facility is located. Notices of self-certification or self-recertification will be published in the Federal Register. An entity filing a good faith notice of self-certification of EWG or FUCO status will be deemed to have temporary status upon filing. If no action is taken by the Commission within 60

[225] Scottish Power Comments at 14. See also EEI Comments at 34, Public Citizen Comments at 6.

days after the date of filing of a self-certification notice, the exempt wholesale generator status or foreign utility company status shall be deemed to have been granted. The Office of the Secretary will periodically issue notices listing the entities whose self-certification of EWG or FUCO status is deemed to have been granted in the absence of Commission action to the contrary within 60 days after the date of filing. We believe that such a self-certification of EWG and FUCO status will be adequate in the vast majority of cases.

227. For entities that require a higher degree of legal certainty as to their status, we will permit them to seek a Commission determination of their EWG and FUCO status as defined under section 366.1 of the Commission's regulations. Specifically, section 366.7(b) provides that they may seek such a determination by filing a petition for declaratory order pursuant to Rule 207(a) of the Commission's Rules of Practice and Procedure justifying the request for EWG or FUCO status. These petitions will be noticed in the Federal Register. A person filing a petition for declaratory order in good faith will be deemed to have temporary EWG or FUCO status until the Commission takes action to grant or deny the petition.

228. The self-certification procedure established herein, along with the continued availability of Commission determinations of EWG and FUCO status, ensures that the EWG and FUCO exemptions will continue to be available to any persons who satisfy the statutory criteria. Moreover, we note that the self-certification procedures established herein, and advocated by various commenters, are less burdensome than the procedures established under section 32 of PUHCA 1935.

229. We disagree with commenters such as Calpine and EEI who argue that Congress,

by incorporating the definition of EWGs and FUCOs into PUHCA 2005, carried over the requirement from PUHCA 1935 that the Commission make case-by-case determinations of EWG status. This argument appears to rest on the erroneous assumption that Congress effectively reenacted (only) section 32(a) of PUHCA 1935. Had Congress meant to do so, it could have simply so stated in PUHCA 2005; alternatively, it could have imported the text from section 32(a) of PUHCA 1935, with appropriate modifications, into section 1262(6) of EPAct 2005, as it did for many of the other definitions carried over from PUHCA 1935. Instead, however, Congress directed that "[t]he terms 'exempt wholesale generator' and 'foreign utility company' have the same *meanings* as in section 32 and 33" of PUHCA 1935 as they existed on the day prior to the date of enactment of EPAct 2005. We believe it is a reasonable interpretation that, even if Congress preserved the option of EWG status determinations going forward, it did not prescribe the procedural mechanics requiring a case-specific Commission ruling on what it means for a person "to be engaged directly, or indirectly through one more affiliates …, and exclusively in the business of owning or operating, all or part of one more eligible facilities and selling electric energy at wholesale." Thus, we conclude that, by repealing section 32 of PUHCA 1935, Congress left to the Commission the discretion to prescribe the procedures for obtaining EWG status.

230. As noted earlier, with respect to FUCOs, section 33 of PUHCA 1935, as amended by EPAct 1992 provided that FUCOs would be exempt from PUHCA 1935 and not deemed an electric utility company, but the exemption would not apply or be effective unless relevant state commission(s) certified that they had the authority and resources to

protect ratepayers of public utility companies associated or affiliated with the FUCO. Given that PUHCA 2005 is largely a books and records statute, we will waive our accounting and reporting requirements for FUCOs. However, we will not exempt them from section 366.2 of our regulations, which allows us to obtain access as necessary with respect to jurisdictional rates. The case-by-case approach that we adopt here is consistent with our precedent concerning the treatment of FUCOs under the FPA and will allow us to ensure adequate protection of captive customers in the United States.

8. Cross-Subsidization and Encumbrances of Utility Assets

231. In the NOPR, we noted that PUHCA 2005 is primarily a "books and records access" statute and does not give the Commission any new substantive authorities, other than the requirement in section 1275 of EPAct 2005 that the Commission review and authorize certain non-power goods and services cost allocations among holding company members upon request. Nor does it give the Commission authority to pre-approve holding company activities. Accordingly, outside the context of reviewing a holding company transaction requiring approval under section 203 of the FPA or a proposed issuance of securities under section 204 of the FPA, the Commission will continue to rely primarily on its ratemaking authorities under sections 205 and 206 of the FPA and sections 4 and 5 of the NGA to protect jurisdictional customers against inappropriate cross-subsidization or encumbrances of utility assets on an ongoing basis.

232. In the NOPR, we also noted that the Commission already has in place, pursuant to the FPA and NGA, certain reporting requirements regarding money pools and cash

management activities that affect jurisdictional companies.[226] Further, in the electric area, we have policies that protect against cross-subsidization occurring as a result of wholesale power sales between affiliates in a holding company system as well as sales of non-power goods and services between such affiliates.[227] In the NOPR, we invited comment on whether, in light of the repeal of PUHCA 1935, the Commission needs to promulgate additional rules or to adopt additional policies to protect against inappropriate cross-subsidization or encumbrances of utility assets, pursuant to our authorities under the FPA and NGA. For example, we asked whether, if it has the authority to do so, the Commission should issue rules regarding public utility holding company diversification into non-utility businesses. Would the Commission have authority to promulgate such rules under its FPA or NGA ratemaking authority? Should the Commission modify its existing cash management rules to apply not only to public utilities, natural gas companies, and oil pipelines, but also to include public utility holding companies? We sought comment on these and any other related issues in order to determine whether, in addition to the regulations being proposed herein under PUHCA 2005, the Commission may need to consider promulgating separate, additional rules under the FPA or the NGA.

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[226] Regulation of Cash Management Practices, Order No. 634, 68 FR 40500 (Jul. 8, 2003), III FERC Stats. & Regs. ¶ 31,145 (June 26, 2003), Order No. 634-A, 68 FR 61993 (Oct. 31, 2003), III FERC Stats. & Regs. ¶ 31,152 (2003).

[227] See Merger Policy Statement, FERC Stats. & Regs. ¶ 31,044 at 30,124-25. See also Heartland Energy Services, Inc., 68 FERC ¶ 61,223 at 62,062-65 (1994); LG&E Power Marketing Inc., 68 FERC ¶ 61,247 at 62,121-24 (1994).