UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Repeal of the Public Utility Holding Company Act of 1935 and Enactment Of the Public Utility Holding Company Act of 2005	Docket No. RM05-32-000

COMMENTS OF THE NATIONAL ASSOCIATION OF
STATE UTILITY CONSUMER ADVOCATES

On September 16 2005, the Commission issued a Notice of Proposed Rulemaking in the above-captioned docket. The Commission seeks public comments on rules implementing the repeal of the Public Utility Holding Company Act (PUHCA) pursuant to Title XII, Subtitle F of the Energy Policy Act of 2005 (EPAct 2005).

The National Association of State Utility Consumer Advocates ("NASUCA") is an association representing 44 state utility consumer advocate offices in 41 states and the District of Columbia. Each of these offices is authorized by the laws of their respective jurisdictions to represent the interests of utility consumers in matters before state and federal regulators and courts. NASUCA and its member agencies have been active in the debate over the restructuring of the electric utility industry testifying on numerous occasions before Senate and House committees considering restructuring legislation, including the repeal of the Public Utility Holding Company Act.

Introduction

PUHCA has been on the minds of consumer advocates since the origins of NASUCA as an organization. In a series of resolutions dating back almost 20 years, NASUCA has urged Congress to exercise the greatest caution in response to efforts to dismantle the consumer protections contained in PUHCA. NASUCA has supported PUHCA repeal only in the context of comprehensive restructuring legislation that includes structural protections designed to guard against market power abuses and to protect consumers.

In 1996 NASUCA resolved that:

> "in considering action affecting regulation or the structure of the electric industry, including PUHCA repeal or reform, Congress should require federal regulatory agencies to: 1) prevent abusive or preferential affiliate transactions, 2) continue oversight and protection over corporate and market structure to prevent abuses to consumers and competition, 3) disallow costs which are not prudent and reasonable from wholesale rates, 4) exercise sufficient regulatory authority to prevent ratepayers from bearing any risk of utility diversification and to prohibit cross-subsidies between regulated and nonregulated subsidiaries." NASUCA Resolution 1996-04

NASUCA has reservations about the repeal of PUHCA contained in EPAct 2005. These provisions, we believe, strip away almost 70 years of essential consumer protections without corresponding enhancements to federal authority or the absence of effective competition. While we address the questions raised in the NOPR, we believe this is just the beginning of the process and more work must be done to protect consumers in this new and experimental regulatory regime.

NASUCA's comments can be summarized as follows:

1. The Commission should recommend an amendment to clarify that holding company systems and state commissions with jurisdiction over gas utility companies and natural gas companies in the holding company systems are included within the scope of Section 1275(b). It is also recommended that the Commission request an amendment clarifying that the Commission is able to enforce the provisions of the subtitle concerning natural gas companies using the powers granted under the Natural Gas Act.
2. The Commission and state commissions should have sufficient access to books and records to protect consumers from holding company abuses.
3. Holding Companies should be required to file cost allocation agreements with the Commission.
4. The pricing of interaffiliate transactions must be consistent with a utility's obligation to protect its customers from unreasonable costs.
5. New structural protections must be created to protect consumers from diversification into nonutility business.

Comments on Specific Sections of the Proposed Regulations

6. 1. The Commission should recommend an amendment to clarify that holding company systems and state commissions with jurisdiction over gas utility companies and natural gas companies in the holding company systems are included within the scope of Section 1275(b). It is also recommended that the Commission request an amendment clarifying that the Commission is able to enforce the provisions of the subtitle concerning natural gas companies using the powers granted under the Natural Gas Act.

The Commission notes that Section 1275(b) of PUHCA 2005 provides for Commission review and authorization of cost allocations for non-power goods or services provided by service companies to public utilities (electric), but does not address the provision of non-power goods or services to gas utility companies and natural gas companies. The Commission requests comments about whether it should recommend an amendment to clarify that holding company systems and state commissions with jurisdiction over gas utility companies and natural gas companies in the holding company systems are included within the scope of Section 1275(b).

NASUCA urges the Commission to recommend such an amendment. Gas utility companies and natural gas companies are included in most of the other sections of PUHCA 2005. Their omission in Section 1275(b) significantly impacts not only the Commission's ability to prevent the cross subsidization of affiliates of public utilities, but also limits the Commission's ability to prevent cross subsidization of affiliates of natural gas companies and effectively eliminates the prior review of the allocation of service company costs to gas utilities.

The Commission notes that PUHCA 2005 does not limit the Commission's ability to conduct after the fact reviews of allocations under Sections 4 and 5 of the Natural Gas Act. However, after the fact review of transactions does not necessarily prevent negative impacts from inappropriate allocations of costs from service companies. Prior Commission review and approval of transactions is necessary to prevent service companies from draining the resources of regulated affiliates prior to declaring bankruptcy.

In its Regulation of Cash Management Practices, RM02-14, Notice of Proposed Rulemaking, August 1, 2002 at page 5, the Commission noted the potential for such outcomes involving cash management agreements: "There is thus a potential for degradation of the financial solvency of regulated entities if non-regulated parent companies declare bankruptcy and default on the accounts payable, advances or borrowings owed to their regulated subsidiaries." Without prior Commission review and authorization of allocations to natural gas companies, the solvency of regulated entities would be at risk through inappropriate payments to service companies.

The omission of gas utility companies and natural gas companies from the Commission's review and authorization of cost allocations from service companies also limits the Commission's ability to prevent the subsidization of public utilities. Many of the current registered holding companies have gas utility companies or natural gas company subsidiaries as well as electric utilities. The omission of gas utility companies and natural gas companies from Section 1275(b) creates the potential for public utilities to limit the Commission's ability to ensure that the rates of public utilities are just and reasonable through the use of transactions involving gas utility or natural gas company affiliates.

Similarly, the Commission's ability to ensure that the rates of natural gas companies are just and reasonable will be limited if the Commission is not able to review and authorize cost allocations from service companies to natural gas companies. Many interstate pipelines are subsidiaries of registered holding companies. The allocations of costs from service companies to natural gas companies should be subject to the same review and authorization as applies to public utilities.

Section 1275(b) allows a state commission to request the Commission to review and authorize the allocation of costs between service companies and public utilities. This section does not allow a state commission to request the review and authorization of costs between service companies and gas utility companies. Prior to repeal, allocations between service companies and gas utility companies have been subject to the jurisdiction of the Securities and Exchange Commission. Unless PUHCA 2005 is amended to allow for state commission's to request review and authorization of service company allocations, the only remedies to state commissions will be an after the fact review of such allocations. As noted previously, such reviews of affiliate transactions do not protect the solvency and financial integrity of gas utilities.

Section 1270 of PUHCA 2005 Act clarifies that the Commission has the same powers to enforce the provisions of the subtitle as are set forth in sections 306 through 317 if the Federal Power Act.

It is also recommended that the Commission request an amendment clarifying that the Commission is able to enforce the provisions of the subtitle concerning natural gas companies using the powers granted under the Natural Gas Act.

2. The Commission and state commissions should have sufficient access to books and records to protect consumers from holding company abuses.

If consumers are to be adequately protected from holding company abuse under this new regulatory regime, the Commission and state commission's access to books and records must be clear and standards commanding access liberally applied. Anything less substantially weakens the protections afforded by the remaining provisions of the Act and could result in substantial harm to consumers.

At the very least, the access granted under Section 1264 (a) supplements and does not supplant the Commission's access under FPA Section 205 and 206 and NGA sections 5 and 6 and from the general provisions of FPA Section 301 and NGA section 8. The Commission notes as much in paragraph three of the NOPR ("…these provisions supplement the Commission's broad authority under FPA 301…"). In addition Section 301, which was not amended by EPAct 2005, states that "nothing in this chapter shall relieve any public utility from keeping any accounts, memoranda, or records in which such public utility may be required to keep by or under authority of the laws of any State."

The Commission should make this unambiguous in its final rule.

The Commission must also establish a "relevance" standard that protects consumers from new risks resulting from previously prohibited structures and transactions. Section 1266(b) requires FERC to exempt certain entities from access obligations when the records are "not relevant to the jurisdictional rates of a public utility." In this NOPR, the Commission "does not propose to categorically exempt classes of entities or transactions described in section 1266(b) from the requirements of section 1264" but proposes to "rely on case-by-case exemptions for additional exemption until we have gained further experience subsequent to the repeal of PUHCA."

Consumer advocates' experience with case-by-case consideration to grant exemption is not good. In many cases, limited time is given to comment on a proposed exemption followed by a quick approval lacking precedent and failing to establish a useful rule. A clear definition of "relevance" that the Commission can use with the expected onslaught of exemption applications will provide guidance to parties seeking exemptions and short circuit arguments that the Commission cannot overturn arrangements negotiated in purposeful ignorance. In addition, it will limit the regulatory costs born by State commissions and Consumer Advocates who are forced to expend limited resources time and time again.

"Relevant" under Section 1264 should be defined to reflect the purpose of the Federal Power Act: consumer protection. Therefore, a corporate relationship or transaction, and the parties thereto, are “relevant” if there is a reasonable possibility the arrangement will injure a utility affiliate in any way resulting in harm to the consumer.

Just as important as the Commission’s access to books and records is state commission access. State commissions will have an important watchdog role to play in the post-PUHCA world. Therefore, the Commission should make it clear that its own access does not preempt state access.

Section 1265(a) grants state commissions data access similar to what Section 1264(a) grants FERC. Section 1265(d) states that the Section 1265(a) rights do not preempt any other access rights. A similar state savings clause does not appear in Section 1264. To prevent future arguments that somehow the federal access provisions of Section 1264 preempt state commission access under Section 1265, the Commission should state explicitly that there is no preemption of differing state laws on books and records. Moreover, the Commission should approach any protective order resulting from a State commission request for information with caution and establish a narrow and high hurdle for those who oppose such requests.

3. Holding Companies should be required to file cost allocation agreements with the Commission.

The Commission asks for comment on:

> “whether, in light of the repeal of PUHCA 1935, holding companies that prior to the repeal of PUHCA 1935 were registered holding companies should be required to file such cost allocation agreements with the Commission under section 205 of the FPA and section 4 of the NGA.”

The allocation of costs can easily lead to the misallocation of costs. Public utilities with captive customers and nonutility affiliates facing competitive pressures have paramount incentives to misallocate costs to cover nonutility affiliate mistakes. Under the Federal Power Act, the Commission has an obligation to insure just and reasonable rates and that obligation did not vanish with the passage of EPAct 2005. Therefore, the Commission should require the filing not only of interaffiliate contracts among corporate affiliates, but of all cost allocation practices between utility and non-utility activities, regardless of the corporate structure involved. The cost allocation filing requirement should apply to all holding companies, not only formerly registered holding companies.

But these FERC-approved allocations should not bind state ratemaking authority. Section 1275(b) provides that where an associate company provides goods and services to an affiliated public utility, the affiliated holding company or a state commission having jurisdiction over the public utility may seek a FERC allocation of the cost to the public utility. At the same time, Section 1275(c) says that "[n]othing in this section shall affect the authority of the Commission or a State commission under other applicable law." Since state commissions have state law authority to set retail rates, including authority to disallow purchase costs deemed unreasonable, Section 1275(c) on its face protects the state from preemption.

NASUCA strongly supports the requirement that holding companies file cost allocation agreements with the Commission under section 205 of the FPA and section 4 of the NGA. These agreements are an essential tool that regulators and consumer advocates use to insure that these allocations of costs do not turn into misallocations of costs that are harmful to consumers.

4. The pricing of interaffiliate transactions must be consistent with a utility's obligation to protect its customers from unreasonable costs.

The Commission asks for comments on:

> "whether the Commission should apply the lower of cost or market standard for the allocation of cost for non-powered good and services, or if we should instead adopt the SEC cost standard."

NASUCA suggests that either standard is applicable depending on the fact situation.

A. **Purchases by the utility from the nonutility should be priced at lower of cost or market.** A utility should not pay to the nonutility affiliate a price exceeding what the utility would have paid if it provided the service itself or prudently purchased on the open market from a third party – or the lower of cost or market. Otherwise, the utility is paying a premium for a service that the utility should be performing at cost.

B. **Sales from a utility to a nonutility affiliate should be priced at higher cost or market.** This is consistent with a utility's obligation to minimize its revenue requirement by realizing full value from all assets, the passing that value on to the ratepayers. In actual practice, the "higher of cost or market" is "market" since the affiliate is unlikely to pay its utility a higher price than it could get elsewhere.

C. **Financial aid to the utility from the holding company or nonutility affiliates should be "lower of cost or market.**" The reasons are the same given for "A" above.

5. New structural protections must be created to protect consumers from diversification into nonutility business.

The Commission seeks 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. Comments should specify what additional rules may be needed and the statutory basis for such rules. For example, if it has the authority to do so, should the Commission 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 seek 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."

NASUCA strongly believes that the Commission should promulgate additional rules and adopt additional policies to protect consumers from cross subsidization and diversification ventures. Utility dealings with, and ventures into, nonutility business have had an abysmal record, resulting in harm to captive customers. A quick review of failed utility ventures into nonutility businesses by Arizona Public Service, Westar Energy, Aquila, Alliant Energy, and Northwestern Public Service highlights the real dangers to captive utility ratepayers of diversification ventures. Structural protections, which are designed to prevent problems before they occur, are necessary because rate setting cannot reverse damage already done. Moreover, because State commissions and consumer advocates have limited resources, a regulatory structure preventing problems saves resources and promotes regulatory efficiency and effectiveness. These protections must be consistent with two basic principles:

1. A customer should not be exposed to a nonutility risk involuntarily. Where a customer is captive and has no purchase options, the risk level associated with nonutility businesses must be zero. Forcing such a

customer to buy a piece of unwanted risk would clearly be deemed by the Commission not to be just and reasonable. In this situation, the proper structural protection would be to prohibit a utility's affiliation with nonutility business, unless there is no risk involved.

2. If a customer has power supply options, dealings between utilities and their nonutility affiliates can be approved if: (a) the information on the risk is fully disclosed; (b) the potential gains to the customer from the affiliation are commensurate with the right; and (c) there can be no possible level of harm so large as to render the utility unable to comply with its duty to provide service reliably and economically.

The Commission should consider adopting a number of structural options including prohibiting utility and nonutility business in the same corporate family; limiting nonutility businesses to those which make the operation of the utility more efficient; and creating a general percentage limit of total system assets to nonutility assets. No matter what options the Commission decides to apply, it should establish an advanced review procedure for acquisitions, which gives all parties adequate time to review and comment on an acquisition.

Conclusion

The repeal of the Public Utility Holding Company Act of 1935 creates a number of new challenges for the Commission and State commissions. For the most part, PUHCA has been a successful check on holding company abuse for almost seventy years.

Although the Act was repealed, the obligation of the Commission and state commissions to protect ratepayers from abuses PUHCA was aim at preventing remains. Therefore, the Commission has a duty to promulgate these regulations in a way that is consistent with the intent of Congress and its duty to promote the public interest as found in the FPA and the NGA. If adopted, the suggestions contained in these comments will aid in fulfilling that obligation. Nevertheless, NASUCA believes the work is only beginning and that the Commission must continue to promulgate additional rules and adopt additional policies to protect consumers who now lack the protections once afforded by PUHCA.

Respectfully submitted,

/s/ filed electronically

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