122 FERC ¶ 61,218
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Suedeen G. Kelly, Marc Spitzer,
Philip D. Moeller, and Jon Wellinghoff.

Southern Company Services, Inc. | Docket Nos. ER08-129-000
ER08-129-001

ORDER ON TARIFF FILING

(Issued March 10, 2008)

1. On October 31, 2007, Southern Company Services, Inc., acting as agent for Alabama Power Company, Georgia Power Company (Georgia Power), Gulf Power Company, Mississippi Power Company, and Savannah Electric and Power Company (collectively, Southern Companies), filed proposed revisions to the formula rates under Southern Companies' Open Access Transmission Tariff (OATT), pursuant to section 205 of the Federal Power Act (FPA).[1] Southern Companies state that the filing was made to implement for billing purposes the accounting and reporting guidance for defined benefit post retirement plans that was issued by the Commission's Chief Accountant on March 29, 2007,[2] and was filed pursuant to a settlement agreement approved by the Commission in 2003 (2003 Settlement).[3] In this order, the Commission accepts, in part, the proposed formula rate revision.

I. Background

2. On October 3, 2003, in the 2003 Settlement Order, the Commission approved a proposed amendment to Southern Companies' OATT to convert their stated rates to comprehensive formula rates, effective May 1, 2003. In the instant filing, Southern

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[1] 16 U.S.C. § 824d (2000).

[2] *Commission Accounting and Reporting Guidance to Recognize the Funded Status of Defined Benefit Postretirement Plans*, Docket No. AI07-1-000 (Mar. 29, 2007), *clarified by Correction to Commission Accounting and Reporting Guidance to Recognize the Funded Status of Defined Benefit Postretirement Plans*, AI07-1-001 (Jan. 16, 2008). (Accounting and Reporting Guidance).

[3] *Southern Company Services, Inc.*, 105 FERC ¶ 61,019 (2003) (2003 Settlement Order). Southern Companies' formula rate is set forth in the Formula Rate Manual in Attachment M of Southern Companies' OATT.

Companies explain that the formula methodology is used to establish rates for network and point to point transmission service. As relevant here, the formula rates accepted in 2003 included amounts recorded in Account No. 165, Prepayments, in rate base. Among the items included in Account No. 165 was a "prepaid pension" asset. Generally a prepaid pension asset results from the earnings on the pension trust fund assets exceeding the pension plan obligations.

3. In the 2003 Settlement Order, the Commission required Southern Companies to submit an Annual Informational Filing and a True-Up Filing, as set forth in Attachment N of the OATT. The Annual Informational Filing is to be filed by November 1 before each upcoming Rate Year and uses projected cost data to calculate charges for transmission services for the next Rate Year.[4] On or before May 1 of the year following the Rate Year, Southern Companies must file a True-Up Filing that recalculates the charges based on actual costs for the Rate Year and provides for any necessary refunds or surcharges. Attachment N also states that "changes to fundamental predicates[5] may necessitate *pro forma* adjustments to the formula rate calculations or changes to the formula rate, which may require changes to the input data, to restore the intent of the formula rate as reflected by such fundamental predicates."

4. In the 2005 True-Up proceeding, South Mississippi Electric Power Association, Alabama Electric Cooperative, Inc., and Southeastern Federal Power Customers (collectively, Customer Group) filed a timely Formal Challenge. Among other things, Customer Group argued that Southern Companies improperly included amounts for prepaid pension balances in Account No. 165, claiming that a recent Commission letter to Florida Power & Light Company specified that such amounts should instead be included in Account No. 186, Miscellaneous Deferred Debits.[6] Consistent with Southern Companies' OATT, the Commission set the issues raised in the Customer Group's Formal Challenge for hearing and settlement judge procedures.[7]

[4] The Rate Year is from January 1 to December 31.

[5] The fundamental predicates are as follows: (i) the FERC Uniform System of Accounts; (ii) the Transmission Provider's accounting policies/practices/procedures; (iii) FERC accounting directives and precedents; and (iv) the ratemaking practices of the transmission provider at the federal and state levels.

[6] Account No. 186 is not included in rate base in Southern Companies' formula rates.

[7] *See Southern Company Services, Inc.*, 117 FERC ¶ 61,308, at P 4 (2006), *reh'g denied*, 118 FERC ¶ 61,141 (2007) (citing Attachment N, section 2). The Commission subsequently issued an Accounting and Reporting Guidance requiring jurisdictional public utilities to record the overfunded assets of its defined postretirement benefit plans (including pensions) in Account No. 129 (Special Funds). *See* Accounting and Reporting Guidance.

5. In 2007, the parties reached a settlement (2007 Settlement), which states in relevant part:

> If, by no later than December 1, 2007, Southern Companies should make a section 205 filing with the Commission seeking authorization to implement the Commission's March 29, 2007 accounting directive issued in Docket No. AI07-1-000 for billing purposes under the OATT formula rate and determination of the appropriate ratemaking treatment of Southern Companies' prepaid pension asset, including any related components, expenses or accounts in the OATT formula rate, than any Commission final order concerning such filing shall apply for the entire 2007 Rate Year, and all subsequent Rate Years until changed by an appropriate order of the Commission, regardless of the date of the Commission's final order. Customer Group and AMEA may seek to intervene and participate individually or jointly as parties to any ensuing proceeding concerning such filing and shall be free to make any arguments regarding the appropriate ratemaking treatment of such pension asset, related components, expenses, or accounts through the sponsoring of testimony or otherwise. [8]

6. In the instant filing, made pursuant to the 2007 Settlement provision excerpted above, Southern Companies propose to include Account No. 129[9] in their formula rates and request waiver of the Commission's notice requirements to allow the OATT change to take effect January 1, 2007.

II. Notice of Filing, Interventions, and Protests

7. Notice of Southern Companies' filing was published in the *Federal Register*, 72 Fed. Reg. 64,205 (2007), with protests and interventions due on or before November 21, 2007. Alabama Municipal Electric Authority (AMEA) and Customer Group filed motions to intervene. Customer Group also filed a protest, motion to require completion of filing, and a request for a hearing and provision for refunds. On December 6, 2007, Southern Companies filed an answer to Customer Group's protest.

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[8] *See* Explanatory Statement in Support of Offer of Settlement Agreement, Appendix A, section II (4), Southern Company Services, Inc., Docket No. ER06-919. The Commission approved the 2007 Settlement by order dated March 6, 2008.

[9] The Commission has since clarified that major electric utilities should use Account No. 128 instead of Account No. 129 to record prepaid pension assets. *See Correction to Commission Accounting and Reporting Guidance to Recognize the Funded Status of Defined Benefit Postretirement Plans*, AI07-1-001 (Jan. 16, 2008).

8. On December 20, 2007, Commission Staff sent a deficiency letter requesting specific information regarding Southern Companies' request to include a prepaid pension asset in rate base. Southern Companies responded on January 9, 2008. Notice of Southern Companies' second filing was published in the *Federal Register*, 73 Fed. Reg. 4202 (2008), with protests and interventions due on or before January 31, 2008. On January 31, 2008, Customer Group filed timely comments and a supplement to its protest. On February 15, 2008, Southern Companies filed a response to Customer Group's comments.

III. <u>Discussion</u>

9. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2007), the timely, unopposed motions to intervene serve to make the entities that filed them party to this proceeding. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2007), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept Southern Companies' December 6, 2007 answer because it has provided information that assisted us in our decision-making process. However, we are not persuaded to accept their February 15, 2008, answer and will, therefore, reject it.

A. <u>Parties' Arguments</u>

1. <u>Southern Companies Initial Filing</u>

10. Southern Companies state that the proposed adjustment to their formula rate will enable them to continue to include in their OATT formula rate an amount that was intended to be captured by the formula rate but will otherwise be excluded upon implementation of the Accounting and Reporting Guidance. Southern Companies further explain that, prior to issuance of the Accounting and Reporting Guidance, they recorded their prepaid pension asset in Account No. 165, Prepayments, which is included in rate base in their formula rate. However, pursuant to the Commission's Accounting and Reporting Guidance, prepaid pension amounts must now be recorded in Account No. 128, which is not currently in Southern Companies' formula rate.

11. Southern Companies state that income earned on pension assets in their external trust was credited back to customers as non-cash reductions to Account No. 926, Employee Pension and Benefits. Further, Southern Companies assert that, as a reduction to an expense account, that amount reduced Southern Companies' cost of service to all customers, including tariff customers, by over $1 billion since 1987. Southern Companies explain that, because they cannot actually withdraw and use the pension income from the external trust account, they must finance these reductions in order to provide them to customers, and therefore the pension asset amount should be included in rate base.

12. Southern Companies state that, because this is a *pro forma* adjustment that will not cause the charges under their OATT formula rate to change, this filing is eligible for abbreviated filing requirements and they need not file testimony and comparative

numbers in support of the adjustment.[10] Southern Companies contend that they are requesting a "rate change other than an increase" and do not seek to add any cost-of-service items or data inputs to the OATT formula rate that are not already included. Accordingly, Southern Companies state that their filing meets the qualifications for a section 205 filing with abbreviated filing requirements. Moreover, Southern Companies state that this filing is in accordance with the filed rate doctrine and the specific procedures in Attachment N, that allow them to adjust their formula rate to maintain the fundamental predicates as they existed on December 31, 2002, when their approved formula rate took effect.

13. If the Commission does not accept the proposed formula rate change, Southern Companies request in the alternative that the Commission also exclude the prepaid pension asset's corresponding cost and income credit elements from the formula rates, which they assert operate together to reduce the overall cost impact of the prepaid pension asset and reduce transmission service charges. Specifically, Southern Companies contend that customers receive the benefits of the pension asset income through a reduction to expenses reflected in Account No. 926, a reduction to cash working capital associated with pension income, and an additional reduction to rate base achieved by virtue of the accumulated deferred income tax treatment of the prepaid pension asset.

2. <u>Customer Group Comments on Initial Filing</u>

14. Customer Group contends that this filing is incomplete because it is not accompanied by the required materials, testimony, and exhibits.[11] Customer Group argues that, under the 2007 Settlement Order, Southern Companies must submit a complete section 205 filing, including testimony to explain their claims regarding offsetting costs related to the prepaid pension asset, as well as their claim that the proposed change is required to reflect the parties' intent at the time the 2003 Settlement was reached. In support, Customer Group notes that the parties to the 2007 Settlement agreed that Southern Companies would file a section 205 filing. Customer Group also argues that the instant filing does not qualify for abbreviated filing requirements because the Commission did not approve the inclusion of prepaid pension costs in the first instance. Customer Group requests that the Commission find Southern Companies' filing deficient and order them to comply with their obligation to meet the burden of presenting a complete case.

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[10] 18 C.F.R. § 35.13(a)(2)(iii) (2007) ("Any utility that files a rate schedule change that does not provide for a rate increase or that provides for a rate increase that is based solely on a change in delivery points, a change in delivery voltage, or a similar change in service, must submit with its filing only the information required in paragraphs (b) and (c) of this section.") Cost of service information is required under paragraph (d), and testimony and exhibits are required under paragraph (e).

[11] *See* 18 C.F.R. § 35.13(e), (g) (2007).

15. Customer Group further asserts that Southern Companies have the burden of demonstrating that the proposed filing will result in just and reasonable rates. Customer Group argues that the Commission's Accounting and Reporting Guidance does not address the ratemaking treatment of these expenses, and that Commission approval can be provided only after review of the rates and charges to determine if they are just and reasonable. Customer Group contends that Southern Companies are improperly attempting to shift the burden of proof to parties challenging the filing and that the parties to the 2003 Settlement never intended for the prepaid pension asset to be included in rate base. Customer Group also disputes Southern Companies' alternative request, arguing Southern Companies did not properly explain the offsetting adjustments that they seek to exclude.

3. Southern Companies' Response

16. In its December 6, 2007 response, Southern Companies cite the documents filed in the proceeding that led to the 2003 Settlement Order and argue that those included a full cost-of-service analysis, which clearly showed inclusion of prepaid pensions in rate base. Moreover, Southern Companies assert that Customer Group's current objection to inclusion of the prepaid pension asset in formula rates, five years after the 2003 Settlement Order, is contrary to the filed rate doctrine and barred by Commission precedent. Southern Companies state that, if Customer Group has an objection, it should file a complaint under section 206 of the FPA.[12]

4. Southern Companies Response to Deficiency Letter

17. In their January 9, 2008 response, Southern Companies continue to assert that their cost of service has been reduced by over $1 billion since 1987 as a result of the income earned on the pension asset. Specifically, Southern Companies state that they record pension income as a "reduction to expense" in FERC Account No. 926, which is part of the data inputs to their formula rates under their OATT.[13] Southern Companies contend that this $1 billion reduction benefits customers because it reduces the total amount of operating expenses included in the calculation of Southern Companies' revenue requirement, which in turn, reduces customer rates. Southern Companies argue that, under their OATT, they true-up rates for each year to actual costs for that year. Thus, there can be no year in which prepaid assets are accumulated but rates are not correspondingly reduced. Southern Companies reiterate that they must finance the amount of the pension income-related reductions through their capital structure and provide an illustration to demonstrate why.[14]

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[12] 16 U.S.C. § 824e (2000).

[13] Southern Companies Response, Attachment C.

[14] Southern Companies' illustration starts with an assumed cash cost of service of $400 before considering pension income. The example then assumes pension income of

(continued…)

5. Customer Group Comments on Response to Deficiency Letter

18. In its January 31, 2008 Comments, Customer Group argues that Southern Companies failed to prove that their customers received an offsetting rate benefit equal to the effect of the inclusion in rate base of the prepaid pension asset going back to 1987. Further, Customer Group contends that Southern Companies did not make annual filings that would reduce customer rates by the amount of the alleged benefit. Customer Group notes that Southern Companies' claim that their cost of service was reduced by the cumulative amount of the alleged benefit, but do not claim that their rates were reduced by that or any other specified amount. Finally, Customer Group argues that the Commission should not be persuaded by Southern Companies' Attachment C, which it claims is "a single page chart" that the Commission and stakeholders are supposed to decipher "to arrive at the conclusion that Southern [Companies have] somehow provided rate reductions."[15]

B. Commission Determination

19. The Commission will accept in part Southern Companies' proposal to revise their formula rates to include amounts in Account No. 128 related to prepaid pensions for billing purposes. [16] As explained below, the Commission will allow Southern Companies to include in their formula rates under the OATT the jurisdictional portion of prepaid pension amounts accrued after May 2003. However, the Commission will not allow Southern Companies to include any other prepaid pension amounts in their formula rates.

1. Abbreviated filing requirements

20. We begin by examining the 2007 Settlement, in which the parties agreed that Southern Companies had the option of making a section 205 filing seeking authorization to implement the Commission's Accounting and Reporting Guidance for billing under

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$100. Netting the $100 of pension income against the $400 of other cost of service items results in a revenue requirement of $300, which the example assumes means that Southern Companies only collects $300 from ratepayers. Because Southern has to pay $400 for the other cost of service items, has only collected $300 from ratepayers, and cannot withdraw and use the pension income from the external trust, it must finance the $100 of pension income from debt and equity capital.

[15] Customer Group Comments at 4.

[16] The Commission has since clarified that major electric utilities should use Account No. 128 instead of Account No. 129 to record prepaid pension assets. *See Correction to Commission Accounting and Reporting Guidance to Recognize the Funded Status of Defined Benefit Postretirement Plans*, AI07-1-001 (Jan. 16, 2008). We therefore will approve the use of Account No. 128 rather than Account No. 129, as proposed.

the OATT and "determination of the appropriate ratemaking treatment of Southern Companies' prepaid pension asset, including any related components, expenses or accounts in the OATT formula rate." If Southern Companies chose to make such a filing, Customer Group and AMEA had the right to make arguments related to the propriety of Southern Companies' proposed ratemaking treatment of such pension asset, related components, expenses, or accounts. In light of this provision, we conclude the 2007 Settlement obligates Southern Companies to support their proposed ratemaking treatment. Southern Companies therefore have an obligation, under the 2007 Settlement, to fully explain the basis for their proposal to include the prepaid pension asset, related components, expenses, or accounts in their formula rate.[17]

2. <u>Prepaid Pension Asset in Rate Base</u>

21. As a general matter, it is appropriate to include prepayments in rate base when they represent amounts that a utility has paid for costs that are allowed to be collected in rates in the future, such as for prepaid insurance or prepaid rent. This is because the utility is out-of-pocket for such costs until they are recovered from ratepayers and is therefore entitled to recover its cost of financing such prepaid expenses. In the instant case, Southern Companies, in essence, are asserting that they are out-of-pocket for $1.1 billion of prepaid pension costs. However, unlike prepaid insurance or prepaid rent, prepaid pensions arise when the income earned on pension funds accumulated in an external trust exceeds the net periodic pension cost, *i.e.*, the current year's pension income exceeds the current year's pension expense. By law, a utility cannot withdraw such income,[18] although it is required (under Generally Accepted Accounting Principles) to reflect the income as a reduction to its pension expense, *i.e.*, as a credit to Account No. 926. At the same time, the utility records a corresponding amount of prepaid pensions.[19] If that reduction in pension expense is used in determining a utility's rates, there will be a corresponding reduction in the amounts collected from ratepayers. Because a utility cannot withdraw the pension income, it will be out-of-pocket for the amount of pension income that has reduced rates, *i.e.*, it must reduce its pension expense by the amount of income, even though it is not allowed to receive such income from the pension trust.[20] Thus, when a utility's rates have been reduced by pension income, but

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[17] Absent the 2007 Settlement, Southern Companies could have merely filed pursuant to Attachment N to reflect changes in a fundamental predicate, *i.e.*, the Transmission Provider's accounting practices, to reflect the accounting changes contained in the Commission's Accounting and Reporting Guidance directive.

[18] In this situation, a pension fund is said to be "over-funded," and such over-funding is expected to be temporary. However, if an external pension fund is over-funded when it is terminated, any excess funds must be returned to ratepayers.

[19] Southern Companies have been recording such prepaid pensions in Account No. 165, but seek to re-classify them to Account No. 129 in the instant proceeding.

[20] *See* illustration in n.14.

the utility has not received such income from the external trust, it will have to finance such amount, and is entitled to include the pension income in rate base. Conversely, if a utility records pension income in Account No. 926 but its rates are *not* reduced, the utility will not be out-of-pocket for the pension income. In this latter situation, the utility is not entitled to earn a return on the prepaid pensions, as it will not actually finance them; therefore, it should not include them in rate base.

22. In the instant case, the Southern Companies have had formula rates in effect for network and point-to-point transmission rates under their OATT since May 2003. Southern Companies' formula rates track amounts recorded in their expense accounts, including Account No. 926. Southern Companies' Attachment C lists, by operating company, the net periodic pension cost or income that was included in Account No. 926 since 1987, the year that they adopted the accounting for pensions under Statement of Financial Accounting Standards No. 87.[21] This Attachment shows that, between 2003 and 2006, Southern Companies reduced their pension expense by $320,623,404.[22] Because Southern Companies' OATT formula rates track the reduction in pension expense resulting from pension income, and therefore result in reduced rates, the Commission concludes that Southern Companies have justified inclusion of the jurisdictional portion[23] of such prepaid pensions in rate base. Therefore, we will accept Southern Companies' filing to the extent that they seek to include the jurisdictional portion of prepaid pension assets accrued since May 2003 in rate base.

23. However, Southern Companies have not justified inclusion of any other prepaid pension amounts that they seek to include in rate base. In its deficiency letter, Commission Staff asked Southern Companies to:

> support your assertion that customers have benefited through rate reductions by over $1 billion and that Southern Companies, in fact, have experienced out-of-pocket costs equal to the amount of prepaid pension assets. This demonstration must include evidence that the amounts included in prepaid pensions actually reduced rates by the same amounts in all years during which the prepaid pensions were accumulated.[24]

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[21] According to Attachment C, net pension income, *i.e.*, credits to Account No. 926, began in 1993.

[22] This amount would be somewhat less than the $320,623,404, since Southern Companies' formula rates were effective only from May 1, 2003 forward.

[23] As used here, the jurisdictional portion is that portion related to amounts reflected in Commission-jurisdictional OATT rates.

[24] Deficiency Letter at 2.

24. In response, Southern Companies state only that the cost of service has been reduced by over $1 billion since 1987 as a result of the income earned on the pension asset. Specifically, they state that the reduction to expense is to Account No. 926, which is a data input for computing rates under their OATT. Southern Companies do not address, either in their original filing, or in their response to Staff's deficiency letter, how amounts included in prepaid pensions actually reduced transmission rates for years prior to May 2003. Southern Companies do not, for example, explain whether their pre-May 2003 transmission rates were based on a formula, like that currently effective under Southern Companies' OATT, or whether pension income in any prior year was used in determining stated transmission rates. Of the $1.1 billion of prepaid pensions that Southern Companies seek to include in rate base, more than two-thirds of that amount relates to periods prior to May 2003. Since Southern Companies have not shown that they reduced transmission rates prior to May 2003 by the jurisdictional portion of that pension income, the Commission cannot conclude that Southern Companies have had to finance any prepaid pensions accrued prior to May 2003. Therefore, the Commission finds that it is not just and reasonable for Southern Companies to include any amounts related to prepaid pensions accumulated prior to May 2003 in rate base under Southern Companies' OATT. Similarly, any corresponding amounts of working capital reductions and deferred income taxes should also be excluded from OATT rate determinations.

25. In accordance with the above findings, we will direct Southern Companies to file within 30 days of the date of this order, revisions to their OATT that: (1) add Account No. 128 (rather than Account No. 129) to those accounts included in their OATT formula rate; and (2) specify that only the jurisdictional portion of prepaid pensions accrued since May 2003 be included in rate base. We will also direct Southern Companies to recompute their 2007 formula rates to reflect this determination.

<u>The Commission orders</u>:

(A) Southern Companies' proposal is hereby accepted in part and rejected in part as discussed in the body of this order, effective January 1, 2007.

(B) Southern Companies are hereby directed to revise their 2007 formula rates as discussed in the body of this order, and make a compliance filing within 30 days of the date of this order to reflect such adjustments.

(C) Southern Companies are hereby directed to recompute their OATT billings to reflect the determinations of this order

By the Commission.

(S E A L)

Kimberly D. Bose,
Secretary.