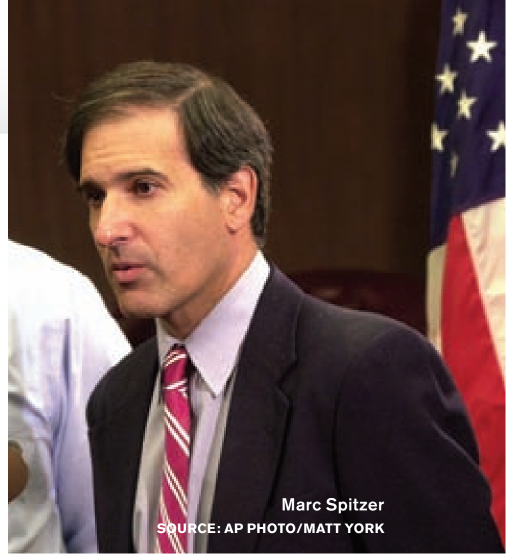
Marc Spitzer
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Infrastructure Needed

STEPS TO ENCOURAGE BUILDING

BY MARC SPITZER

THE NATION'S UTILITY GRID HAS BEEN STRAINED by increased demands, which hinders both competition and reliability. These strains have been exacerbated by the lack of building electric infrastructure. Recognizing this, Congress included section 1224 in the energy act of 2005 to give the Federal Energy Regulatory Commission authority to grant entities incentives to invest in transmission infrastructure. In Order No. 679, FERC established criteria, consistent with a congressional directive, to grant the incentives. In general, FERC requires entities seeking incentives to show that the project will ensure reliability or reduce congestion. Entities seeking incentives must also show that there is a nexus between the incentive sought and the proposed project and that the project is not routine. While utilities may not receive incentives for every new transmission facility, such as for routine facilities, since passage of the energy act of 2005 the commission has granted incentives to several utilities that have demonstrated that the incentives will result in a robust and reliable transmission facility.

New infrastructure also is needed for the nation's interstate oil and natural gas pipeline system. The commission is grappling with two contentious rate issues that impact investment and whether much-needed investment in the interstate pipeline grid will be adequate in the future – the grant of an income tax allowance and the inclusion of master limited partnerships in the comparative "proxy group" for fixing return on equity.

In 2005, the commission issued a policy statement that concluded that a pass-through regulated entity would be permitted an income tax allowance if its partners had an actual or potential income tax liability on the jurisdictional income of a pass-through entity.

The return on equity a pipeline is able to earn is based on the return that other similar companies – otherwise known as a proxy group – earn. Historically, the entities included in a proxy group were companies whose pipeline operations constituted a high proportion - at least 50 percent - of the company's business. However, the proliferation of MLPs in the energy sector has resulted in a paucity of these proxies for natural gas pipelines. Consequently, the determination of the types of entities to be included in a natural gas pipeline's proxy group is an issue the commission now confronts.

The 2007 ruling of the U.S. Court of Appeals for the D.C. Circuit, ExxonMobil Oil Corp. v. FERC, provides insight on both the grant of an income tax allowance and the inclusion of MLPs in a proxy group. In ExxonMobil, the court approved the commission's grant of an income tax allowance to SFPP, an interstate oil pipeline structured as an MLP. In doing so, the court affirmed the commission's conclusions in its 2005 policy statement. According to the court, there was no legitimate reason to restrict the income tax allowance to corporations, given that "both partners and Subchapter C corporations pay income taxes on their first tier income."

In recognition of this case law, the commission issued a proposed policy statement concerning the composition of the proxy groups used to determine gas and oil pipelines' return on equity. Further, the commission recently requested additional comments solely on the issue of MLP growth rates to supplement the existing MLP policy statement record because the record did not adequately address how to project MLP growth rates, if the commission ultimately decides to permit the use of MLPs in the proxy group. As such, the commission's review of this issue is ongoing.

To facilitate competitive markets, the commission's policies must foster attractive returns on investments in electric and natural gas infrastructure. Successful resolution of these issues will facilitate the transportation of our nation's supply of reliable, affordable energy.

Marc Spitzer is a member of the Federal Energy Regulatory Commission.

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