Transource Response to PJM Artificial Island Supplemental Proposal Request

September 12, 2014

Executive Summary

Transource is pleased to provide the supplemental information regarding its Salem-North Cedar Creek 230 kV Proposal (P2013_1-2B) in response to PJM's Artificial Island Supplemental Proposal Request issued on August 12, 2014. Transource, using the extensive resources and experience of its parent company American Electric Power Company ("AEP"), has undertaken significant additional due diligence to firm up both the cost of the project and to examine the technical aspects and constructability of the project. This additional work was undertaken in coordination with recognized industry-leading firms that have extensive experience in executing similar projects: ABB (submarine line provider), Prysmian (submarine line provider), Caldwell Marine International (submarine line construction firm), Burns & McDonnell (substation and line engineering and construction) and Terracon (geo-technical analysis).

Based upon our further efforts and analysis, Transource is providing a revised project cost that it is willing to stand behind through a meaningful cost containment mechanism. In addition, Transource has confirmed that there is no change to the estimated project duration of four years.

Transource is supplementing its proposal with the following information:

- Transource and Pepco Holdings, Inc. ("PHI"), parent company of Delaware incumbent utility Delmarva Power and Light Company ("Delmarva"), have executed a Memorandum of Understanding pursuant to which, upon the satisfaction of certain conditions, the parties would jointly develop, construct, operate and maintain the project if it is awarded to Transource. This arrangement significantly improves the likelihood of project success based on PHI/Delmarva's significant experience working in the project area, familiarity working with the numerous permitting agencies and on-the-ground resources to provide operations and maintenance services over the life of the project. PHI/Delmarva's experience and resources are an outstanding complement to the extensive resources and experience of AEP in delivering large, complex transmission projects on-time and on-budget. This

arrangement also eliminates the uncertainties associated with the Delaware public utility regulations referenced in the Artificial Island Supplemental Proposal Request.

- Transource has received letters from two Delaware property owners indicating they are prepared to negotiate the private rights of way necessary for the project. The remaining right of way would be on publically-owned lands.

- Transource's revised project cost is $203.0 million exclusive of contingency and work required at the Salem station[1]. The project cost increase is primarily attributable to the following: (i) the need, identified by Caldwell Marine International, to use specialized construction techniques (horizontal directional drilling and cofferdams) for portions of the submarine cable, (ii) the inclusion of a spare installed underwater cable required by PJM and (iii) revised permitting, right of way and wetland mitigation costs.

- Through its additional due diligence, Transource has also developed a project contingency of $52.3 million. [REDACTED]

- Transource is proposing a cost containment mechanism that provides a financial incentive for Transource to deliver the project at or below its project cost. Transource is willing to forego all or a portion of the FERC awarded return on equity incentives (including the RTO participation adder) on project costs exceeding the revised project cost of $203.0 million.

[1] Cost estimate for work at Salem generating station is $46.0 million. In addition, the project cost does not include any costs, which are expected to be immaterial, associated with modifications to the Red Lion, Cartanza and Cedar Creek substations where the existing 230 kV lines terminate.

Benefits of Transource/PHI Joint Participation

Transource and PHI have executed a Memorandum of Understanding pursuant to which, upon the satisfaction of certain conditions, the parties would jointly develop, construct, operate and maintain the project if it is awarded to Transource. This arrangement significantly improves the likelihood of project success based on PHI/Delmarva's significant experience working in the project area, familiarity working with the numerous permitting agencies and on-the-ground resources to provide operations and maintenance services over the life of the project. PHI/Delmarva's experience and resources are an outstanding complement to the extensive resources and experience of AEP in delivering large, complex transmission projects on-time and on-budget.

The joint participation of Transource and PHI/Delmarva provides substantial tangible benefits to the overall success of this project including the long term operation and maintenance of the system. Transource will rely on the experience and resources of PHI/Delmarva for aspects of the rights of way acquisition, permitting and licensing, and system operation and maintenance. PHI/Delmarva's presence in Delaware as a transmission utility provides this project with exceptional benefits.

PHI/Delmarva has transmission and substation engineering and maintenance, project management, environmental, real estate, telecommunications, construction management, transmission planning and transmission operation organizations dedicated to planning, constructing, maintaining, operating and repairing transmission facilities. They have unique knowledge of the Delmarva transmission system; familiarity with the local communities; experience in building, and specific experience in maintaining and siting transmission facilities in these communities. PHI/Delmarva has successfully acquired electrical rights of way for numerous projects. In addition, they have successfully navigated the risks associated with the permitting of environmentally challenging areas, including river crossings and wetlands. PHI/Delmarva has extensive coastal facilities and regularly manages the unique challenges associated with tidal wetland, salt air environment and coastal environment. Their personnel have successfully coordinated public outreach campaigns for similar projects in the Delmarva Peninsula.

PHI/Delmarva also is experienced with providing system operation and maintenance services for similar systems within the area. This includes first responder and storm restoration capabilities from nearby facilities. PHI/Delmarva maintains in-house crews, equipment and material to quickly restore

transmission and substation facilities 24 hours a day, seven days a week. Delmarva's Newark, Delaware 24 hour operations center is located approximately 15 miles away from the proposed North Cedar Creek substation and can quickly provide boots on the ground for emergency services. In addition, they have a comprehensive overhead and underground inspection program and capability to address, resolve or mitigate any issues identified.

Notwithstanding the Delaware Public Service Commission vote on Tuesday, September 9, 2014, the Commission's order does not resolve the Delaware statutes and other regulatory requirements that may limit the ability of non-incumbents to build transmission facilities in Delaware. The joint participation of Transource and PHI/Delmarva resolves these uncertainties as set forth in the legal opinion from Morgan Lewis included in Appendix A.

In addition, other federal, state and local siting and permitting requirements, such as those required by the Army Corps of Engineers and Delaware Department of Natural Resources and Environmental Control, will need to be satisfied. Transource believes that the Transource-PHI joint participation leverages the project development strengths and local system knowledge and expertise needed to successfully navigate and address these federal, state and local siting and permitting requirements and statutory restrictions.

Private Property Land Access

Burns & McDonnell investigated land ownership data in the vicinity of the project and engaged with private landowners to determine their willingness to negotiate rights of way on their property. Burns and McDonnell identified that rights of way on private property was only required from two Delaware landowners for the project. Transource subsequently procured letters from the two Delaware landowners indicating they are prepared to negotiate the private rights of way necessary for the project. These two private rights of way enable Transource to identify a viable line route and substation site in Delaware, with the remaining required right of way for the project on publically owned lands. Appendix B contains a summary of Burns & McDonnell's work. Appendix C contains a confidential property ownership map with the applicable properties identified. The referenced letters from property owners are attached as Appendix D and E.

Updated Project Cost

The complexities of the project (scenic and environmentally sensitive area, river soil conditions, etc.) and the uncertainty associated with the Delaware and New Jersey siting and permitting processes has made providing "final terms of project costs" challenging. In response to PJM's request, Transource has updated the project cost based on the significant additional due diligence performed by Transource and AEP in coordination with recognized industry-leading firms that have extensive experience in executing similar projects: ABB (submarine line provider), Prysmian (submarine line provider), Caldwell Marine International (submarine line construction firm), Burns & McDonnell (substation and line engineering and construction) and Terracon (geo-technical analysis).

Transource's revised project cost is $203.0 million, exclusive of work required at the Salem station[2] which we assume will be designated by PJM to the incumbent transmission owner. The revised project cost increase is primarily attributable to the following: (i) the need, identified by CMI, to use specialized construction techniques (horizontal directional drilling and cofferdams) for portions of the submarine cable to meet expected permitting requirements, (ii) the inclusion of a spare installed underwater cable required by PJM and (iii) revised permitting, right of way and wetland mitigation estimates. The revised project cost is displayed by cost components in the table below:

[2] Cost estimate for work at Salem generating station is $46.0 million. In addition, the project cost does not include any costs, which are expected to be immaterial, associated with modifications to the Red Lion, Cartanza and Cedar Creek substations where the existing 230 kV lines terminate.

(all 2014 dollars)	
Description of Cost Item	**Estimate**
Permitting/Routing/Siting	4,000,000
ROW/Land Acquisition	2,000,000
Wetland Mitigation	9,500,000
Submarine Line EPC	158,613,055
Overhead Line EPC	7,433,799
New Delaware Substation EPC	12,500,000
Project and Construction Management	2,000,000
Owner Directs	1,000,000
Owner Internal Overheads	5,911,406
TOTAL PROJECT COST	**202,958,260**
* EPC = Engineering, Procurement and Construction	

ABB and CMI have completed extensive work to analyze the submarine portion of the project, provided an updated cost estimate and confirmed the project schedule; this work is detailed in Appendix F. ABB is one of the most experienced suppliers and installers of polymer ("XLPE") insulated high voltage and extra high voltage submarine and upland cable systems in the world and CMI is highly experienced in constructing similar submarine line projects in the United States. More recently, ABB and CMI working together supplied, installed and commissioned the first 345 kV XLPE insulated submarine cable system in North-America: i.e.; the Bayonne Energy Center project across the lower Hudson River (New York Harbor) between Bayonne, New Jersey, and Brooklyn, New York. Transource also received indicative pricing for manufacturing and delivery of the submarine cable from Prysmian, another major supplier of such materials.

Based upon their extensive experience, ABB and CMI believe the submarine line portion of the project is constructible and permittable. However, to protect the environmentally sensitive area, permitting the project will likely require special construction approaches, which are the major drivers of the cost. These include installation using horizontal directional drilling on both sides of the river to

minimize excavation of the river bed. Submarine installation using horizontal directional drilling limits environmental impact and facilitates safe working conditions. In addition, the horizontal directional drilling requires construction of in-water cofferdams to contain drilling fluids. The two horizontal directional drilling segments, including cofferdams, account for 75% of the revised cost for construction of the submarine line portion of the project. The estimate also includes route clearance costs so that obstacles that may be encountered can be removed. Transource believes that these special construction approaches will be required for permitting any submarine project in this area.

Project Contingency Cost

Transource has identified a project contingency of $52.3 million. [REDACTED]

Cost Containment Mechanism

Transource's offers a cost containment mechanism for the project that provides substantial financial incentive for Transource to deliver the project at or below its revised project cost. Under the cost containment mechanism for this project:

(a) Transource would be entitled to recover its FERC approved return on equity plus incentives on the costs it incurs for the project up to its revised project cost of $203.0 million exclusive of contingency costs;

(b) Transource would forego fifty percent (50%) of any return on equity incentives approved by FERC (including the RTO participation adder) on that portion of the costs incurred for the project that exceed the revised project cost of $203.0 million but that are less than the revised project cost plus contingency of $255.3 million; and

(c) Transource will forego one hundred percent (100%) of return on equity incentives approved by FERC (including the RTO participation adder) on that portion of the costs incurred for the project that exceed $255.3 million.

These estimates are in 2014 dollars and would be adjusted for inflation based on the Consumer Price Index and appropriate commodity and/or foreign currency exchange rates, if applicable. Excluded from the cost containment mechanism is (i) cost for work required at the Salem station which Transource assumes will be designated by PJM to the incumbent transmission owner and (ii) any costs associated with modifications to the Red Lion, Cartanza and Cedar Creek substations where the existing 230 kV lines terminate.

APPENDIX A

MEMORANDUM

Morgan Lewis
COUNSELORS AT LAW

TO: Amanda Riggs Conner

FROM: Colm F. Connolly
Levi McAllister
Amy M. Dudash

DATE: September 12, 2014

SUBJECT: Delaware Statutory and Regulatory Requirements Regarding Construction of Transmission Facilities and Use of Eminent Domain

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You have asked us to analyze applicable Delaware law governing the construction of transmission facilities in Delaware and to determine whether Transource Delaware Inc., working in conjunction with Pepco Holdings, Inc. ("PHI"), could obtain property through the exercise of eminent domain. This memorandum addresses each of those issues.

As we discuss below:

- The Delaware Public Service Commission ("DPSC") and the Delaware courts take a broad view in interpreting the definition of public utility. As a result, it is possible that Transource Delaware, working in conjunction with PHI, would be deemed a public utility. However, a reasonable argument exists that Delaware's public utility definition is intended to apply only to entities that provide retail service within Delaware, and that Transource Delaware thus is not a public utility. We believe this latter argument is the stronger argument, but we have not found any dispositive precedent on the issue. Thus, we believe that Transource Delaware, working in conjunction with PHI, could make filings with the DPSC seeking to operate as a public utility or may also be deemed to be an unregulated non-public utility.

- If Transource Delaware is deemed a public utility, it would become subject to the regulatory oversight of the DPSC. If it were subject to that oversight, Transource Delaware would be required to seek and obtain a certificate of public convenience and necessity ("CPCN") from the DPSC in order to operate as a public utility.

- If Transource Delaware is a public utility, the DPSC will have eminent domain authority to obtain rights of way. Whether or not Transource Delaware is a public utility, it will have a public right-of-way through canals, rivers, waterways, and along state highways, and an ability to initiate condemnation proceedings with any owner that is burdened.

- If Transource Delaware is not deemed a public utility, it may still be possible for Transource Delaware to construct its proposed transmission facilities. The DPSC has issued a declaratory order concluding that Delaware law does not prohibit

nonincumbent transmission developers from constructing and owning facilities in Delaware. However, the DPSC's September 2014 order is subject to reconsider and judicial review. As discussed below, current Delaware law providing that electric distribution companies shall have the exclusive right to furnish transmission and distribution services to all electricity-consuming facilities located within its service territory introduces some uncertainty as to whether a nonincumbent transmission only company will be able to construct transmission facilities within a Delaware public utility's service territory.

- If Transource Delaware is not deemed a public utility, even working in conjunction with PHI, Transource Energy may structure the project such that those portions requiring public utility status could be developed and owned by Delmarva Power, an existing Delaware public utility and subsidiary of PHI.

I. Background

In April 2013, PJM Interconnection, L.L.C. ("PJM") issued a request for proposals seeking proposed solutions to improve the operational performance in the Artificial Island geographic region of New Jersey, which consists of the Salem #1, Salem #2, and Hope Creek #1 nuclear generation facilities. In response to its request, PJM received 26 proposed solutions from seven possible developers. Among those, Transource Energy ("Transource") proposed four possible solutions:

- Transource 2A – Expand the Cedar Creek substation in Maryland, and develop a new substation near Artificial Island and a submarine line under the Delaware River. The expected cost of the project is between $219 million and $269 million.

- Transource 2B – Build a new substation near Artificial Island, a submarine line under the Delaware River, and a new substation in Delaware that will tap the existing 230 kV Red Lion—Cartanza and 230 kV Red Lion—Cedar Creek lines. The estimated cost of this project is between $165 million and $208 million.

- Transource 2C – Upgrade the Salem and Red Lion substations, and construct a 500 kV Red Lion—Salem line from Delaware to New Jersey. The estimated cost of the project is between $123 million and $156 million.

- Transource 2D – Install a new 500 kV New Freedom—Lumberton—North Smithburg line from New Jersey to Pennsylvania. The estimated cost of the project is $994 million.

Transource 2A, Transource 2B, and Transource 2C each involve the construction of transmission facilities in Delaware that would be used to transmit energy to or from New Jersey. In each of those proposals, Transource advised PJM that Transource would form two new subsidiaries, Transource New Jersey, LLC and Transource Delaware, to own the required facilities in the respective states.

With respect to Transource 2D, Transource's proposal does not involve the construction of transmission facilities in Delaware and Transource would not form Transource Delaware.

Because Transource 2D does not involve construction in Delaware, it is not germane to the remainder of this memorandum.

We understand that two options are being considered for the development of the proposals. First, Transource Delaware is considering developing one of its proposals in conjunction with PHI, although the precise arrangement is yet to be determined. Second, if Transource Delaware is unable to obtain public utility status in the state of Delaware, Transource Delaware may structure the project such that Delmarva Power may develop and own that portion of the project requiring public utility status.

II. Discussion

A threshold question to this analysis is whether Transource Delaware would be a public utility in Delaware. We thus first address whether an owner and operator of transmission facilities in Delaware that transmits energy, but does not provide retail service, is a public utility subject to regulation by the DPSC. We then describe the DPSC requirements applicable to public utilities that own and operate transmission facilities in Delaware. Third, we analyze whether a company may develop transmission facilities in Delaware if the owner and operator of the facilities is not deemed a public utility subject to regulation by the DPSC. Fourth, we evaluate whether exclusive service territory rules in Delaware could preclude construction of transmission facilities in Delaware that transmit energy outside of the state. Finally we consider whether rights-of-way necessary to construct transmission facilities in Delaware may be obtained through eminent domain.

A. Characterization as a Public Utility

A threshold question that must be resolved in considering the implications of and requirements for constructing transmission facilities in Delaware is whether Transource Delaware would be deemed a public utility.

Pursuant to Title 26 of the Delaware Code, the DPSC exercises "exclusive original supervision and regulation of all public utilities and also over their rates, property rights, equipment, facilities, service territories and franchises."[1] As defined by the Delaware Code, a "public utility" includes:

> [E]very individual, partnership, association, corporation, joint stock company, agency or department of the State or any association of individuals engaged in the prosecution in common of a productive enterprise (commonly called a "cooperative"), their lessees, trustees or receivers appointed by any court whatsoever, that now ***operates or hereafter may operate for public use within this state*** . . . any natural gas, electric (excluding electric suppliers as defined in § 1001 of

[1] 26 Del. C. § 201(a).

> this title), water, wastewater, . . . telecommunications . . . service, system, plant or equipment.[2]

In analyzing the definition of public utility, Delaware precedent considers two questions: (i) whether the entity operates or hereafter may operate within Delaware; and (ii) whether operations are for the public use within Delaware. The DPSC and the Delaware courts take a broad view in applying the definition of public utility, which creates a possibility that Transource Delaware would be deemed a public utility. However, a reasonable argument exists that Delaware's public utility definition is intended to apply only to entities that provide retail service within Delaware. We believe the latter position is the stronger of the two.[3]

1. Operates or Hereafter May Operate

Courts and the DPSC have addressed the "operates or hereafter may operate" clause of the public utility definition in one instance. However, a 2006 DPSC opinion (the "Utility Systems Opinion") applied an expansive interpretation to the clause while concluding that a wastewater plant was a public utility because it operated in Delaware.[4] This Utility Systems Opinion appears to be the only case where the "operates or hereafter may operate" clause of the statue has been interpreted.

In the proceeding that gave rise to the opinion, the owner of wastewater transport facilities argued that it was not "operating" in Delaware because the owner of the wastewater facilities only transported wastewater and did not engage in the treatment of the transported wastewater. The DPSC disagreed. In its ruling, the DPSC determined that the owner of the wastewater facilities fell within the public utility definition because the owner had facilities in Delaware that were covered by the public utility definition (i.e., wastewater transport facilities).[5]

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[2] *Id.* § 102(2) (emphasis added).

[3] Neither the DPSC nor the Delaware courts have considered whether an entity is a public utility if that entity owns and operates facilities in Delaware but does not serve Delaware customers. Rather, Delaware precedent is limited to circumstances where an entity serves customers within Delaware through its facilities. In this regard, we note that an argument can be made that energy transmitted over the new transmission facilities may be consumed in Delaware. Even if energy is not purchased directly from the facilities for retail customers, to the extent energy is sold into the PJM market that energy is then commingled and arguably sold throughout the PJM region. However, we do not view this issue – whether or not energy transmitted over the new transmission facilities is consumed in Delaware -- to affect the analysis of this memorandum because Transource Delaware would not be the retail service provider even if energy transmitted over Transource Delaware's facilities were sold into the PJM market and later sold throughout the PJM, including into Delaware. Transource Delaware will not sell energy to retail customers. Moreover, Transource Delaware will not provide unbundled retail transmission service; any purchase from PJM markets to serve load in Delaware will be made at the load bus as a wholesale purchase.

[4] *In the Matter of the Commission's Investigation, on its own Motion, Whether Utility Systems, Inc., Operates as a Public Utility in its Ownership, Operation, and Maintenance of a Wastewater Collection System Serving the Henlopen Station Condominium Properties Near Rehoboth Beach, Delaware*., Order No. 7009, Del. PSC (Aug. 22, 2006) .

[5] *Id* at 24.

The DPSC affirmed a hearing examiner's conclusion that "[t]he plain meaning of the word 'operate' is broad in scope" and that the term means "to perform a function."[6] The DPSC determined that the wastewater plant operated within Delaware because its transport of wastewater constituted "performing a function" in Delaware. In addition, the DPSC deemed the wastewater plant to be operating for the purpose of the public utility definition because the owner of the wastewater plant was responsible for the maintenance and repair of the lines used to transport wastewater.[7]

Finally, the DPSC affirmed the hearing examiner's rejection of the wastewater facility owner's argument that transport of wastewater through pipes, by itself, should not trigger the public utility definition. The hearing examiner whom the DPSC affirmed explained:

> According to USI, any company, including a regulated wastewater utility, could construct the largest wastewater transport pipelines in the State, extending for hundreds of miles, and as long as it did not treat the wastewater that flows through the pipes, the activity would be exempt from regulation. USI's interpretation would thus lead to absurd results.[8]

It is important to note, however, that unlike the facilities involved in the Transource proposals, the facilities at issue in the Utility Systems Opinion were solely within Delaware and were used to transport the wastewater produced by Delaware residents.

2. Public Use

Delaware courts and the DPSC have placed greater emphasis on the "public use" clause of the public utility definition than the "operates or hereafter may operate" clause. The Delaware Supreme Court has explained that "the pivotal question is the meaning of the phrase 'for public use' in the definition of a public utility," and has applied a "public interest" test when analyzing the public use clause.[9]

The public interest test turns on whether an entity's activities have a significant impact on the public interest that the DPSC was designed to protect – preserving and promoting indispensable services while preventing inferior service with excessive and discriminatory rates.[10] Applying that test, Delaware precedent explains that "regardless of whether a company sells to less than the general public, when a company engages in the sale of a regulated commodity to independent third parties, the selling entity may be subject to the jurisdiction of

[6] *Id* at 34.

[7] *Id.*

[8] *Id.* at 37.

[9] *Eastern Shore Natural Gas Co. v. Delaware Public Serv. Comm'n*., 637 A.2d 10, 15-16 (Del. 1994).

[10] *Id.*; *see also Public Water Supply Co. v. DiPa squale*, 735 A.2d 378 at 383-84 (Del. 1999).

the [D]PSC" as a public utility.[11] This rule also extends to "any operation that affects the public," i.e., it is not limited to sales of a commodity such as energy.[12] For example, the *Reserves* court concluded that a sale is deemed to occur if a third-party is paying for transport rather than the item being transported. In *Reserves*, the court found a sale to a third party when homeowners paid for the service of transporting water even though the homeowners owned the water that was transported. The court stated that "[t]he homeowners would be paying for the service of a water system much in the same way that they would pay for other utilities, such as electricity or telephone service, where no property is actually transferred but essential services are provided."[13]

With respect to whether a sale has a significant impact on the public interest, Delaware precedent distinguishes between services and sales made available to the public and those that are exclusively for the provider's own use. In the former instance, a finding of impact to the public interest is likely to be made because the public otherwise has no recourse to any governmental agency for potential complaints.[14] In the latter, the service may be classified as a private use that is excluded from regulation.[15] The DPSC has endorsed the view of the New Jersey Board of Public Utilities in this regard, explaining that "[i]n interpreting the term 'public use,' as a criterion for regulated 'public utility' status, only those operations that are wholly private are excludable; any service offered to the public or any operation that affects the public will be considered to be within the meaning of 'public use.'"[16]

3. Analysis

Because the DPSC and the Delaware courts take a broad view in applying the definition of public utility, it is possible that Transource Delaware, working in conjunction with PHI, would be deemed a public utility. However, a reasonable argument also exists that Delaware's public utility definition is intended to apply only to entities that provide retail service within Delaware.

Under the existing interpretation of the "operates or hereafter may operate" clause of the public utility definition, the DPSC likely would view Transource Delaware's construction and operation of transmission facilities in Delaware as "operating" for the purpose of the public utility definition. In the Utility Systems Opinion, the DPSC and the hearing officer adopted a broad reading of the clause and found that it applied because the wastewater transport facilities were physically located within Delaware. While, as noted, the facilities at issue were solely

[11] *The Reserves Development Corp. v. Delaware Public Serv. Comm'n.*, Case No. 02A-07-001 HDR at *8 (Del. Super Ct. 2003), *affirmed Reserves Development Corp. v. State PSC*, 2003 Del. LEXIS 436 (Del. 2003) ("*Reserves*").

[12] *In the Matter of Donnelley Directory v. Diamond State Telephone Co.*, Delaware Public Serv. Comm'n, Docket No. 296-89 (1989) (citing *South Jersey Gas Co. v. SunOlin Chemical Co.*, 544 A.2d 402 (N.J. Super. 1988).

[13] *Id.*

[14] *Id.*

[15] *In the Matter of Donnelley Directory v. Diamond State Telephone Co.*, Delaware Public Serv. Comm'n, Docket No. 296-89 (1989) (citing *Re N.B. Partners*, 98 P.U.R. 4th 67, 72 (W. Va. 1988).

[16] *Id.* (citing *South Jersey Gas Co. v. SunOlin Chemical Co.*, BPU Docket No. G08702-82 (N.J.B.P.U. 1987).

within Delaware and were used to transport the wastewater produced by Delaware residents, the rationale of the DPSC applies equally to facilities that arguably are used to transport a commodity either into Delaware and subsequently to the PJM market or to customers outside of Delaware.

Application of the "public use" clause of the public utility definition to the facts here is less clear. Drawing on existing precedent, either the DPSC or a Delaware court could conclude that Transource Delaware's construction and operation of transmission facilities meets the public use test. First, the transmission of energy through Delaware on transmission facilities located in Delaware is akin to the provision of water that the court in *Reserves* addressed; Transource Delaware's transmission of energy would be a sale to a third party even if Transource Delaware is not the producer or seller of the energy it transmits. Second, as noted, the DPSC has endorsed a broad view that only those operations that are wholly private are excludable; any service offered to the public or any operation that affects the public will be considered to be within the meaning of public use (provided they are the types of services identified in the applicable statute, e.g., electric service, water service, or natural gas service). Here, an argument could be made that the construction of the transmission facilities and transmission of energy affects the public because Transource Delaware's facilities are not wholly private.

That being said, a distinguishing factual characteristic exists between applicable precedent and Transource Delaware's proposal since Transource Delaware, even if working in conjunction with PHI, will not be providing retail service to Delaware residents. Although the public utility definition is not specifically limited to entities providing retail service in Delaware, Delaware precedent has only addressed circumstances where an entity utilizes its facilities to serve customers within the state. Neither the DPSC nor the Delaware courts have explicitly considered whether an entity is a public utility if that entity owns and operates facilities located within Delaware but does not provide retail service to Delaware customers.

Currently, Delmarva Power, a retail service provider, is the only regulated electric industry public utility in Delaware. Following the enactment of the Electric Utility Restructuring Act of 1999 ("1999 Restructuring Act"), the DPSC's jurisdiction was curtailed. As the DPSC recognizes:

> In 1999, the General Assembly passed legislation restructuring the electric industry in Delaware. Prior to restructuring, the generation, transmission, and distribution of electric power by investor-owned utilities was fully regulated by the [D]PSC. With restructuring, the generation of electric power became deregulated, leaving only distribution services under the regulatory control of the [D]PSC. The pricing of electric transmission is regulated by the Federal Energy Regulatory Commission (FERC).[17]

Notably, the DPSC here appears to concede that is does not have jurisdiction over *any* transmission service.

[17] Role of the Commission, Delaware Public Service Commission, *available at* http://depsc.delaware.gov/electric.shtml.

Further, independent power producers ("IPPs") have historically avoided regulation as public utilities by the DPSC even though they operate within Delaware.[18] That appears to be because IPP's do not make retail sales to customers in Delaware.[19]

The lack of clarity in the law can be seen by comparing two separate initiatives. On the one hand, a 2003 Delaware Energy Task Force led by then-DPSC Chair McRae, formed in response to Delaware Executive Order No. 31, undertook an examination into the status of transmission capacity in Delaware and the need and feasibility of upgrading capacity and developing new natural gas pipelines. Among other things, the Task Force report noted that "Delaware law appears to classify merchant transmission as a 'public utility', which would require licensing and certification by the Public Utility Commission." In support of this statement, the Task Force report cited, without elaboration, the definition of public utility in Title 26 of the Delaware Code.[20]

On the other hand, in June 2014, Representative Kowalko of the Delaware House of Representatives introduced House Bill 387, which would have required that all transmission service providers obtain "a certificate of public convenience and necessity for the construction and operation of any new electric transmission lines operating at 100KV or greater and located in the State or offshore waters and integrated with the State electric transmission grid." This Bill appears to be premised on an understanding that current law does not provide for DPSC jurisdiction over transmission providers or transmission facilities developed by independent transmission companies, which may or may not also be merchant transmission facilities. House Bill 387 was tabled in the House Transportation/Land Use and Infrastructure Committee on June 5, 2014, and the Delaware General Assembly (both the House of Representatives and Senate) has recessed until January 2015.

While there does not appear to be dispositive precedent, we believe the stronger argument lies with the position that Transource Delaware is not a public utility because Transource Delaware will not use its facilities in Delaware to provide retail service to Delaware customers. We believe this to be the case even though Transource Delaware would be working with an affiliate of an existing Delaware retail electric provider, since the pertinent fact is that

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[18] *In the Matter of the Application of Delmarva Power & Light Company to Use Competitive Bidding to Purchase Capacity and Energy from Non-Utility Generators*, PSC Docket No. 88-34 (Nov. 20, 1989) (characterizing independent power producers and qualifying facilities as "non-utilities").

[19] We note that more recently, the DPSC's jurisdiction has been further narrowed. Following the 1999 Restructuring Act, "the public interest no longer require[s] the generation, supply, and sale of electricity (including all related facilities and assets) to be regulated as a public service or function." *See In the Matter of the Application of Delmarva Power & Light Company, Atlantic City Electric Co., and Conective Delmarva Generation, Inc.*, Order No. 5561, PSC Docket No. 00-238 (Oct. 17, 2000). Likewise, entities that certify as retail Electric Suppliers with the DPSC are also outside of the jurisdiction of DPSC regulation even though those entities make retail sales. *See* 26 Del. C. § 202(f) ("[T]he Commission shall have no supervision or regulation over any electric supplier."). An Electric Supplier is "a person or entity certified by the Commission that sells electricity to retail electric customers utilizing the transmission and/or distribution facilities of a nonaffiliated electric utility." *Id.* § 1001(14). Electric Suppliers must certify to the Commission and satisfy a delineated set of requirements set forth in the Delaware Administrative Code.

[20] Transmission & Distribution Working Group, Delaware Energy Initiative at 20 (Apr. 8, 2003), *available at* http://depsc.delaware.gov/2003tanddfinalrpt.pdf.

Transource Delaware will not provide service to retail customers in Delaware.[21] More generally, such a conclusion is consistent with the DPSC's own view of its jurisdiction following the 1999 Restructuring Act, where the DPSC appears to concede in a description of its authority that it has no jurisdiction over transmission. That being said, to the extent treatment as a public utility provides benefits from a business perspective—including the additional eminent domain authority discussed below—we believe that Transcource Delaware, working in conjunction with PHI, could in good faith make filings with the DPSC to operate as a public utility. Transource Delaware could argue that it is filing because it believes it is a public utility, but that even if it is not, it believes it has the authority to construct transmission facilities (for the reasons discussed in Section C below). We note that DPSC Staff asserted in a September 4, 2014 memorandum provided to the DPSC that Northeast Transmission Development, LLC, a sponsor that proposed developing transmission facilities in Delaware in response to PJM's request for Artificial Island proposals, appeared to meet the public utility definition set forth in the Delaware Code.[22] However, the DPSC Staff did not provide a basis for its position.

B. DPSC Requirements Imposed on Public Utilities

If Transource Delaware were deemed a public utility, it would become subject to the regulatory oversight of the DPSC and would be required to seek and obtain a CPCN to operate as a public utility.[23]

Section 203A of the Delaware Code provides that:

> [N]o individual, copartnership, association, corporation, joint stock company, agency or department of the State, cooperative, or the lessees, trustees or receivers thereof, shall begin the business of a public utility nor shall any public utility begin any extension of its regulated public utility business or operations without having first obtained from the Commission a certificate that the present or future public convenience and necessity requires or will require the operation of such regulated public utility business or extension.[24]

[21] As noted, notwithstanding our conclusion, we believe that a good faith argument could be made that Transource Delaware is a public utility. To make that argument Transource Delaware would assert that the transmission facilities and transmission of energy affects the public in Delaware. Whether working in conjunction with PHI could help support such an argument would depend on the specific arrangements entered into, e.g., whether under those arrangements an argument could be made that Transource Delaware's portion of the transmission facilities can be used by the other party to serve the public in Delaware, and thus is not wholly private.

[22] Memorandum of the Staff of the Delaware Public Service Commission, Delaware Public Serv. Comm'n, Docket No. 14-0297 at 3 (Sep. 4, 2014), *available at* http://depsc.delaware.gov/Agenda%2009-09-14/14-0297%20memo.pdf.

[23] We note in this regard that a CPCN is not, as it is in many other jurisdictions, permission to construct a jurisdictional facility. It instead is a requirement for a company to operate as a public utility.

[24] 26 Del. C. § 203A(a)(1).

The DPSC reserves sole discretion as to whether to grant a certificate.[25] A certificate application would need to demonstrate that the public interest would be served through issuance of a CPCN. In addition, the Delaware Code requires that "[e]very application for a [CPCN] shall include a proposed tariff for approval by the Commission."[26]

In exercising its discretion, the DPSC would likely consider whether the public convenience and necessity is served through the development of facilities that do not serve Delaware citizens. House Bill 387, which proposed to amend Section 203A of the Delaware Code, provides guidance on how the DPSC might evaluate a CPCN application. House Bill 387, had it been adopted, would have required the DPSC to consider:

- The need for the proposed transmission line;
- The impact on the reliability of the transmission grid;
- The long term viability of the public utility proposing the line;
- The technical engineering and operating expertise of the public utility;
- The technology and design proposed for the new transmission line; and
- The economic and safety impact of the proposed transmission line.

As noted above, House Bill 387 was not adopted. We nonetheless believe that it provides guidance as to the types of factors the DPSC would likely consider when determining whether or not to grant a CPCN for a transmission-only company.

C. Development Feasibility for Non-Public Utilities

If Transource Delaware is not deemed a public utility, it may still be possible for it to construct its proposed transmission facilities.[27] In that circumstance, it could do so without the need for a CPCN to operate as a public utility, or any other approval from the DPSC. However, current Delaware law providing that electric distribution companies shall have the exclusive right to furnish transmission and distribution services to all electricity-consuming facilities located within its service territory introduces some uncertainty as to whether a nonincumbent transmission only company will be able to construct transmission facilities within a Delaware

[25] *Del. Coach Co. v. Pub. Serv. Comm'n of Del.*, 265 F. Supp. 648, 652 (D. Del. 1967) ("The term 'public convenience and necessity' has long been recognized as a term of art, the application of which involves the exercise of administrative discretion."); *E. Shore Nat. Gas*, 637 A.2d at 1281 (discussing broad discretion that the DPSC exercises over the decision whether to grant certificate of public necessity).

[26] 26 Del. C. § 301(a). As noted earlier, the rates for transmission service over Transource Delaware's proposed facilities would be subject to approval by the Federal Energy Regulatory Commission, not the DPSC. The tariff requirement of Section 301 of the Delaware Code further supports an argument that public utility status and the need to obtain a CPCN is limited to those entities that provide retail service in Delaware pursuant to rates that are regulated by the DPSC.

[27] Although a possibility, we note that Transource Delaware's proposals submitted to PJM assumed that it would become a public utility in Delaware and seek a CACN.

public utility's service territory. Further, the availability of eminent domain as a method for acquiring the necessary land rights would be limited, as discussed below.

We have found no statutory provision or administrative regulation exists that generally limits construction of transmission facilities to public utilities.

However, we understand that the DPSC, in a June 11, 2014 email to PJM, expressed its view that an independent transmission company may not develop transmission facilities in Delaware. In the DPSC's view, Delmarva Power is the only entity permitted to develop transmission facilities.[28] The DPSC cited only to a statutory provision concerning exclusive service territories and the provision of retail service.

Pursuant to Section 203B of the Delaware Code, the DPSC has established exclusive service territories throughout Delaware within which "public utilities providing retail electric service shall have the obligation and authority to provide retail electric service."[29] Section 203B provides a public utility with the exclusive ability to provide retail service within its service territory. Under Section 203B(g) of the Delaware Code:

> The exclusive retail electric service territories heretofore established by the Commission pursuant to this section shall continue as exclusive service territories for the transmission and distribution of electricity. Except as otherwise provided herein, each electric distribution company shall have the exclusive right to furnish transmission and distribution services ***to all electricity-consuming facilities located within its service territory*** and shall not furnish, make available, render or extend its transmission and distribution services ***to a consumer located within the service territory of another electric distribution company***; provided that any electric distribution company may extend or construct its facilities in or through the service territory of another electric distribution company, if such extension or construction is necessary for such company to connect any of its facilities or to serve its customers within its own service territory. As of the implementation dates as set forth in § 1003(b)(1) and (2) of this title [repealed], there shall be no exclusive service territories for the supply of electricity, except as otherwise herein provided.[30]

In its June 11, 2014 email to PJM, the DPSC expressed its view that this provision of the Delaware Code and the existence of exclusive service territories preclude independent transmission companies from developing facilities in Delaware in connection with the Artificial

[28] Email from Robert Howatt, Delaware Public Service Commission, to PJM (Jun. 11, 2014) ("It is Staff's opinion that only Delmarva Power has the right to furnish transmission and distribution services within its retail jurisdiction. The construction and operation of an Independent Transmission Company in Delaware seems to be foreclosed by statute.").

[29] 26 Del. C. § 203B.

[30] 26 Del. C. § 203B(g) (emphasis added).

Island project. The DPSC cited Section 203B(g) of the Delaware Code and stated "[i]t is Staff's opinion that only Delmarva Power has the right to furnish transmission and distribution services within its retail jurisdiction. The construction and operation of an Independent Transmission Company is Delaware seems to be foreclosed by statute."[31]

On August 29, 2014, Northeast Transmission Development, LLC filed an expedited request for a declaratory order addressing whether the Delaware exclusive service territory statute prevents an independent transmission company from constructing transmission facilities. On September 9, 2014, the DPSC approved an order finding that the exclusive service territory statute does not preclude construction by an independent transmission company.[32]

However, the issue is not free from doubt. Prior to August 29, 2014, no precedent existed in Delaware interpreting the statute and addressing whether exclusive service territories relate only to facilities constructed for the purpose of providing retail service. Further, a DPSC order filed in response to Northeast Transmission Development, LLC's request is subject to reconsideration and/or judicial review. As such, the issue is not settled. To, the contrary, it may be argued on appeal that Section 203B(g) is designed to apply to all facilities developed in Delaware because those facilities provide energy into the PJM market, which is then later provided to Delaware retail customers. As such, a court could determine that the interest of Delaware retail customers requires that all development within Delaware is covered by Section 203B(g), and that service providers within Delaware exclusive service territory are the only permissible transmission developers because they are subject to the regulatory oversight of the DPSC.

D. Eminent Domain Authority

If Transource Delaware were to pursue construction of any of its proposals, limited eminent domain authority would be available to acquire certain rights-of-way that may be necessary to proceed with construction.

As a general matter, eminent domain authority is not available to private entities to acquire rights of way. Rather, private entities are generally required to obtain rights of way through negotiations with land owners for the purchase of property or the acquisition of easements.[33]

The use of eminent domain in Delaware is typically a tool that is held by an agency. Under Delaware law, no agency "shall use eminent domain other than for a public use."[34] Public use is defined to include, *inter alia*, "[t]he use of land for the creation or functioning of public

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[31] *See supra* n.28.

[32] Aaron Nathans, PSC OKs non-Delmarva Transmission Line, Delaware Online, Sep. 9, 2014, *available at* http://www.delawareonline.com/story/money/business/2014/09/09/psc-oks-non-delmarva-transmission-lines/15351399/.

[33] *See, e.g.*, Constructability Analysis of Artificial Island Delmarva Peninsula Project Proposals, UC Synergetic, LLC, (Apr. 30, 2014), *available at* http://www.pjm.com/~/media/committees-groups/committees/teac/20140519/20140519-delmarva-peninsula-lines-constructability-analysis.ashx.

[34] 29 Del. C. § 9501A(b).

utilities, electric cooperatives, or common carriers."[35] In addition, Title 29 of the Delaware Code specifies that eminent domain is available to "state and local land acquisition programs or projects in which federal, state or local funds are used."[36]

Under Title 29, Transource Delaware is not permitted to exercise eminent domain authority. The DPSC could do so on Transource Delaware's behalf if Transource Delaware were deemed a public utility.[37] In that circumstance, the DPSC could exercise its eminent domain authority after concluding that eminent domain is necessary. Further, the DPSC would be required to establish by clear and convincing evidence that the use of eminent domain complies with the definition of public use, i.e., that the condemned land will be used for the functioning of a public utility.[38] On the other hand, if Transource Delaware were not deemed to be a public utility, the DPSC would not be permitted to exercise eminent domain on Transource Delaware's behalf.

Given this, if Transource Delaware is not deemed a public utility, even working in conjunction with PHI, Transource Delaware may pursue an alternate arrangement under which Delmarva Power would develop and own the facilities for which eminent domain authority is needed. In such a case, the DPSC would need to determine that eminent domain is necessary for the functioning of the public utility. Neither the Delaware courts nor the DPSC have analyzed eminent domain authority in the context of determining whether the authority was being pursued to advance the functioning of the public utility. However, to the extent the public utility could show that the transmission facilities will enhance the reliability of the retail service that public utility provides or allow the public utility to transmit power it will sell to its retail customers, an argument may be made that the exercise of eminent domain is warranted in order to ensure that the public utility joint venture member is well-positioned to provide reliable service to its retail customers in Delaware.

Finally, with or without public utility status, as a Delaware corporation, Transource Delaware would have a limited eminent domain authority available to it through Title 26 of the Delaware Code. Section 901 of Title 26 grants Delaware corporations with a public right-of-way to construct transmission lines in certain instances. Section 901(a) states:

> Any telegraph corporation, any telephone corporation or ***any corporation using lines or wires for the transmitting of electrical current***, whether created by prior special act or organized under Chapter 1 of Title 8, ***may erect, construct and maintain its*** telegraph or telephone lines or its ***wires for transmitting electrical current and the necessary fixtures for the same through and across or under any of the canals and canal lands, rivers or other waters and also along any highways within the limits of this State***, outside of highways within the limits of and maintained by

[35] *Id.* at § 9501A(c)(2).

[36] *Id.*

[37] No precedent supports an argument that Transource Delaware could be characterized as a common carrier.

[38] 29 Del. C. 9501A(d).

> incorporated cities and towns, subject to the approval or authority of the public authority having charge or control of such highways and also subject to the right of the owners of the fee on such highways and to the owners abutting upon such highways to full compensation to the extent that their property is taken or burdened.[39]

Section 901(b) provides:

> Whenever any such corporation cannot agree with any such owner as to purchase or damages, the corporation may proceed for the condemnation of any such franchises, easements, canals, canal lands, rivers or other waters or highways or burdens imposed upon landowners abutting upon any highways.[40]

Thus, section 901 would appear to grant Transource Delaware with a public right-of-way through canals, rivers, waterways, and along state highways, and with an ability to initiate condemnation proceedings with any owner that is burdened.

[39] 26 Del. C. § 901(a) (emphasis added).

[40] *Id.* at § 901(b).

APPENDICIES B - F

[REDACTED]