

*Transmission Cost Allocation:*  
*The Seventh Circuit Decision and The  
Proposed Corker Amendment*

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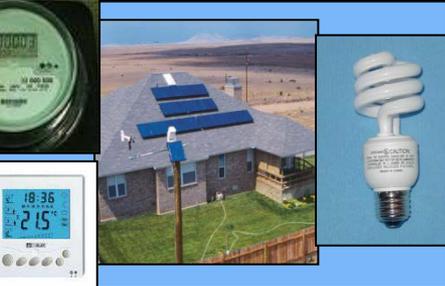
# American Electric Power

## Strength & scale in assets & operations

❖ 5.1 million customers in 11 states.

❖ Largest Transmission Owner in the US with 2,100 miles 765kV

Asset	Size	Industry Rank
Domestic Generation	~38,400 MW	#2
Transmission	~39,000 miles	#1
Distribution	~208,000 miles	#1

Generation	Transmission	Distribution		Customers
				
<ul style="list-style-type: none"> <li>• Environmental Projects</li> <li>• Wind</li> <li>• IGCC</li> <li>• Carbon Capture &amp; Storage</li> </ul>	<ul style="list-style-type: none"> <li>• I-765™</li> <li>• Electric Transmission Texas JV</li> <li>• Electric Transmission America JV</li> <li>• AEP-ABB Alliance</li> </ul>	<ul style="list-style-type: none"> <li>• Distribution automation</li> <li>• Self-healing distribution circuits</li> <li>• Advanced metering</li> <li>• Communications infrastructure</li> <li>• Mobile workforce</li> <li>• Internal energy efficiency</li> <li>• Integration platform for advanced visualization and analytics</li> <li>• Distributed generation and energy storage</li> </ul>		<ul style="list-style-type: none"> <li>• Customer programs and incentives                             <ul style="list-style-type: none"> <li>• Energy efficiency</li> <li>• Direct load control</li> <li>• Peak demand reduction</li> </ul> </li> <li>• Energy storage</li> </ul>
Existing generation and transmission control systems	gridSMART <sup>SM</sup> : bridging the gap to provide integrated two-way communications & control across the electricity value chain		Home energy automation	

# Seventh Circuit Decision

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- ❑ *Illinois Commerce Commission v. Federal Energy Regulatory Commission* held that FERC's decision to provide for PJM-wide allocation of the costs of new 500+ kV transmission projects was not adequately supported by FERC's general claims of widespread benefits in the form of improved reliability and reduced congestion. 576 F.3d 470 (7th Cir. 2009).
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- ❑ Important to take a careful read of the decision and appreciate what the court said and what the court did not say with respect to FERC's responsibilities on considering and approving cost allocation methodologies.
    - Held that FERC was required to allocate costs, in fixing a just and reasonable cost allocation policy under section 206, based on consideration of "cost-causation" and "beneficiary pays" principles.
    - Found that the record developed in this case failed to make an adequate linkage between the distribution of benefits from new transmission investment projects and the distribution of costs for those projects and remanded the issue to FERC for further consideration.

# Seventh Circuit Decision

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## Noteworthy Excerpts.....

- ❑ [As] far as one can tell from the Commission's opinions in this case, the likely benefit to Commonwealth Edison from new 500kV projects is zero. The opinion on rehearing attributes the need for new transmission capacity in PJM to the threat of "degraded reliability in Eastern PJM," and nowhere do the Commission's opinions suggest that degraded reliability is a danger in Midwestern PJM. [1]
- ❑ We do not suggest that the Commission has to calculate benefits to the last penny, or for that matter to the last million or ten million or perhaps hundred million dollars. *Midwest ISO Transmission Owners v. FERC, supra*, [373 F.3d 1361, 1369 (D.C. Cir. 2004)] ("we have never required a ratemaking agency to allocate costs with exacting precision"). If it cannot quantify the benefits to the midwestern utilities from new 500 kV lines in the East, even though it does so for 345 kV lines, but it has an articulable and plausible reason to believe that the benefits are at least roughly commensurate with those utilities' share of total electricity sales in PJM's region, then fine; the Commission can approve PJM's proposed pricing scheme on that basis. For that matter it can presume that new transmission lines benefit the entire network by reducing the likelihood or severity of outages. But it cannot use the presumption to avoid the duty of "comparing the costs assessed against a party to the burdens imposed or benefits drawn by that party." [2]

[1] *ICC v. FERC*, 576 F.3d 470, 476 (7th Cir. 2009) at 476-77 (citations omitted).

[2] *Id.* at 477 (some citations omitted).

# Options for FERC after the *ICC v. FERC* Decision

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- ❑ ***Develop a record supporting the original decision.*** FERC has the option on remand of attempting to quantify and flesh out the general benefits of 500+ kV lines identified in the RTEP process, and using that record to support PJM-wide cost allocation for all of the 500+ kV project costs.
- ❑ ***Modify PJM tariff to require a quantitative benefits analysis and assignment of costs based on that analysis.*** FERC could require PJM's cost allocation for new 500+ kV lines be on the basis of a benefits analysis, and provide direction about how benefits (e.g., reliability benefits, improved integration of renewable generation resources, reduced congestion, and improved options for buyers and market opportunities for sellers in wholesale markets) should be assessed in the analysis.
- ❑ ***Issue General policy or rulemaking.*** FERC could take a more expansive approach, and pursue a generic rulemaking on how to perform a benefits analysis in a reasonably standardized manner that will minimize the need for case-by-case litigation.

# Cost Allocation Methodologies-Post August 6<sup>th</sup>, 2009

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## What Should RTOs Consider As They Develop or Revise Transmission Cost Allocation Policies?

Until FERC provides further guidance, RTOs have latitude to make judgments as to:

- Whether benefits are assessed for individual projects or aggregated packages of transmission investments;
- Time horizon over which costs and benefits are considered;
- Type of benefits considered (which might include, for example, benefits associated with reduced congestion and lower generation costs, reliability benefits, the ability to bring renewable energy to load centers, local economic development, the ability to meet future greenhouse gas regulations, and land conservation benefits associated with use of extra-high voltage facilities); and
- The uncertainties in projecting benefits.

The *ICC v. FERC* decision does not mandate that FERC or RTOs adhere to a one-size-fits-all approach on benefits analysis and cost allocation. Nor does it require detailed analysis through production cost models without consideration of other benefits. FERC's obligation on remand in reviewing and approving cost allocation proposals from RTOs, is to ensure that there is a reasonable consideration of benefits, an explanation of the relationship between the benefits and cost allocation decisions through a clear record. (Smith/O'Daugherty November 6, 2009)

# Corker Amendment

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## Original

- ❑ (B) May permit allocation of costs for high-priority national transmission projects to load-serving entities within all or a part of a region, except that costs shall not be allocated to a region, or subregion, that are **disproportionate to reasonably anticipated benefits**;

## Senator Corker

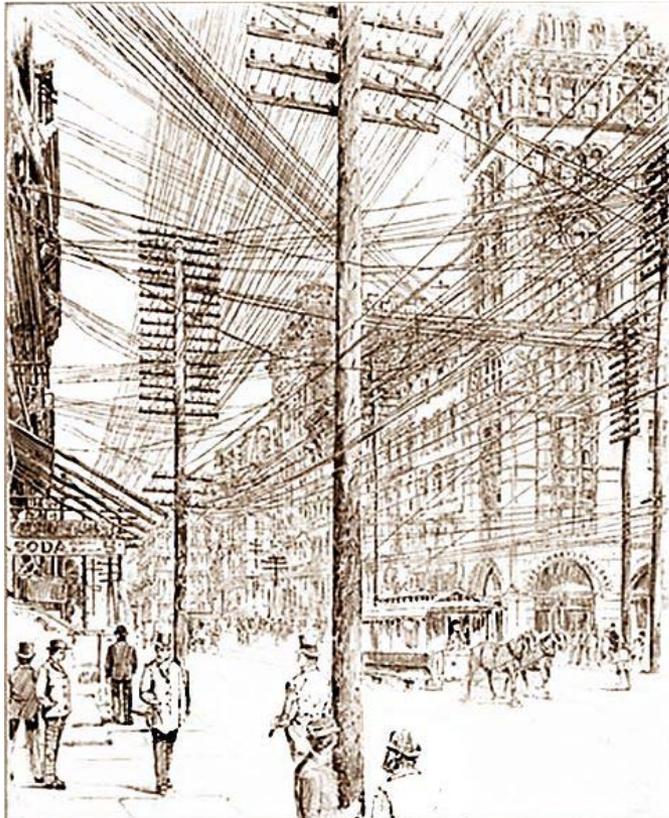
- ❑ (B) May permit allocation of costs for high-priority national transmission projects to load-serving entities within all or a part of a region, except that costs shall not be allocated to a region, or subregion unless the costs are reasonable proportionate to measurable economic and reliability benefits;
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## Result of the Amendment:

- ❑ Prohibits the allocation of costs to a region or subregion unless the costs are “reasonably proportionate to measurable economic and reliability benefits.”
- ❑ Arguably moves the standard beyond beneficiary pays model to a standard which requires proof well beyond a reasonable doubt and inherently limits the scope of possible beneficiaries. Erodes concept of administrative authority and discretion.
- ❑ Adoption will result in lower voltage transmission development, development of radial facilities, HVDC and MORE, less efficient transmission.

# Looking Forward: If Corker Amendment is Successful?

- ❑ Rigid cost benefit analyses which evaluate the system on a “line by line” basis are not in keeping with today’s needs to build and support a robust backbone grid and fail to capture the full system benefits.
- ❑ Corker amendment will encourage the development of single purpose transmission facilities.



Eastern RTO planning processes based on “Production cost” studies generally do not assess important benefits:

- Enhanced market competitiveness
- Enhanced market liquidity
- Economic value of reliability benefits
- Added operational and A/S benefits
- Insurance and risk mitigation benefits
- Capacity benefits
- Long-term resource cost advantage
- Synergies with other transmission projects
- Impacts on fuel markets
- Environmental and renewable access benefits
- Economic benefits from construction and taxes

These omitted transmission-related economic benefits, often doubling benefits from production cost studies make formulaic beneficiary-pays cost allocation approaches unworkable. *(Brattle Group: December 1, 2009)*

# Toll Roads vs. Open Access



- ❑ If RTO's fail to develop long term solutions on a timely basis, the market will provide its own solutions.
- ❑ Bypassing tradition RTO for cost allocation/recovery will encourage the development of other models:
  - Merchant lines
  - Merchant anchor tenant
  - HVDC preference
- ❑ Nature of non-traditional models will result in lines that are at capacity as soon as they are constructed.
- ❑ The Result: More (not less) transmission will be built; greater consumption of ROW; less efficient transmission and a more costly energy delivery system for consumers.

- ❑ Development of an open access robust system will provide the broadest system-wide benefits and flexibility over the long term
- ❑ We cannot afford to limit the quantification of benefits to production cost savings and reliability benefits.
- ❑ The grid is an investment in infrastructure. Siting transmission will not get any easier, we need to consider all the benefits, not just those that are easy to calculate.
- ❑ The United States needs to follow other countries in the development of a robust integrated grid.



The best storage facility for energy is an integrated grid without bottlenecks.

# Looking Forward: If Seventh Circuit Prevails?

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- ❑ Basic framework for Commission action on cost allocation remains the same.
  - Commission ratemaking decisions continue to be governed by the just and reasonable standard in sections 205 and 206 of the FPA, the need to adhere to procedural requirements to explain its decisions and rely on substantial evidence in the record for its findings are found in the Administrative Procedures Act.
- ❑ RTOs developing transmission cost allocation policies after the seventh Circuit decision are not limited to considering only those benefits that can be easily quantified.
  - While the court required that FERC present some analysis of benefits beyond a mere presumption, the court continues to adhere to the policy that “exacting precision” is not required. The court even remarked that the calculation of benefits need not be precise to “the last million or ten million or perhaps hundred million.” [ These comments indicate that the court was primarily concerned with the failure of FERC to create *any* record supporting its conclusion that all PJM members would benefit from 500+ kV lines. It did not find that wide-spread benefits of high-voltage transmission projects do not exist.
- ❑ In support of the recognized need for FERC to establish a clear record which rationalizes and explains the Commission’s decision, RTOS should articulate and highlight the full range of benefits.
  - RTOs are not limited to relying on “production cost benefits.” Although these are typically the benefits easiest to quantify, the Seventh Circuit did not limit the required consideration of benefits to such generation cost savings. Thus, RTOs should provide FERC with whatever analysis of project benefits, and the distribution of those benefits, it has produced in the planning and related RTO processes.

(Smith/O’Daugherty November 6, 2009)

# The Future??

40 Years of the US Interstate Highway System: An  
Analysis  
The Best Investment A Nation Ever Made

*A Tribute to*

*The Dwight D. Eisenhower System of Interstate  
& Defense Highways*

*By*  
*Wendell Cox & Jean Love for the  
American Highway Users Alliance*

*June 1996*

Right: Excerpts from the 1996 report > >

## Impact on the Economy

- ❑ “The interstate highway system has had a profound effect upon the American economy and contributed significantly to improved economic efficiency and productivity.”
- ❑ “... estimates have been made of the contribution of the interstate highway system to the economy, generally finding that the interstate highway system has more than paid for itself in improved commercial productivity... it is estimated that the interstate highway system is now producing approximately \$14 billion in annual producer cost reductions. Over the 40 year period, it is estimated that gross producer cost reductions have exceeded \$1 trillion --- more than three times the gross original investment in the interstate highway system.

40 years from now what will industry treatises say about the decisions that we made in 2010? *An example of leadership and foresight....or protectionism and parochialism? The choice is ours.....*

# References

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- ❑ *ICC v. FERC*, 576 F.3d 470, 476 (7th Cir. 2009).
- ❑ "Transmission Investment Needs and Cost Allocation: New Challenges and Models"  
*The Brattle Group presented to: Federal Energy Regulatory Commission Staff,*  
*December 1, 2003*
- ❑ "Transmission Cost Allocation Policies After Illinois Commerce Commission v. FERC: RTOs and FERC Retain Substantial Discretion" *Douglas W. Smith and Patrick O. Daugherty, November 6, 2009*