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Transmission Planning and Expansion
Pricing Proposals for Network Upgrades and Expansions
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The market signals provided through locational marginal pricing (LMP) and the award of Congestion Revenue Rights (CRRs) provide the incentive framework for market-driven upgrades and expansions. Market driven investments benefit customers by shifting the risk of bad investment onto the professional risk managers in the financial community. This is one of the primary benefits of moving to a market-based system. Getting this market framework in place along with a complementary regional planning process should be the priority for the Commission.

Market-oriented regional planning provides a distinction between (1) investments that the market is willing to pursue and (2) investments that are justified, but the market is not willing to pursue for some reason. In the latter case, there may be some market failure; such as the presence of substantial free rider problems or that a particular reliability problem is not priced, so there is no incentive structure to stimulate the necessary responses from the market. This requires an administrative backstop to ensure that justified investments are made, and there must be a designated “builder of last resort” that is allowed and required to undertake the necessary investments. Here, the regional planning process can help identify these projects and ascertain that they are justified and confirm that the market is not able or willing to undertake them. However, even for “backstop” investments, costs should be assigned to those who benefit, and beneficiaries may include generators, loads, or other market participants. Only where beneficiaries cannot be precisely defined should costs be assigned to all loads on a rolled in basis. This last option should be used sparingly so as not to undermine the benefits that can be derived from the market.

Pricing for upgrades and expansions should be done on the following basis and in the following order:

- Market based investments, including those for congestion relief, should be funded by participants.
- For backstop investments costs should be assigned to beneficiaries to the extent that they can be identified.
- If no specific beneficiaries can be identified, only then should costs be rolled in.

The following matrix illustrates how these principles can be applied.

	<u>Market-Driven Participant Funded</u>	<u>Regulated Beneficiary Funded</u>	<u>Regulated Rolled Into Access Charges</u>
LMP/CRR Incentives (including congestion relief) drive investments	Market Builds There are enough benefits for voluntary, non-regulated investment	Intervention probably not needed; Pre-empts market-driven investment	Intervention harmful; Pre-empts market-driven investment; subsidizes beneficiaries; leads to non-economic investments; undermines LMP
LMP/CRR Incentives Don't Drive Investment, Beneficiaries Can Be Identified, Investment is Still Justified	Not enough benefits for voluntary or free rider problem	Builder of Last Resort Beneficiaries pay; discourages free-riders	Non-beneficiaries subsidize those who benefit; encourages free riders
LMP/CRR Incentives Don't Drive Investment, Beneficiaries Cannot Be Identified, Investment is Still Justified	Not enough benefits for voluntary or free rider problem	N/A (cannot charge specific beneficiaries since they aren't defined)	Builder of Last Resort Intervention okay; costs rolled in as last resort as part of system access charge (everyone pays)

As the matrix illustrates, the regional planning process must adjust accordingly away from the old "command and control" structure, such as integrated resource planning, to a role of accommodating market-driven investments. To do otherwise dampens the benefits that markets can bring. This of course assumes there is a market structure with incentives in place to drive investments, specifically LMP and CRRs.

In order for market-driven investment to thrive, the planning process must be coordinated by an entity that is truly independent of any reason to bias a planning outcome. To have a competitor squarely in the center of the decision-making process with perfect information would have a chilling effect on competitively derived solutions.

Where core features of the Standard Market Design are working, such as PJM, these principles are being successfully applied. The focus on market-driven solutions with an administrative backstop has helped to ensure that necessary transmission investment is occurring in the region while still delivering the benefits of competitive markets.