Competitive Transmission Development Rates Technical Conference

Docket No. AD16-18-000

Panel 1: Cost Containment Provisions in Competitive Transmission Development Processes

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*About the Speaker*

Mr. Smyth is the President of Transource Energy, LLC ("Transource"), which is a transmission-focused joint venture of American Electric Power Company, Inc. ("AEP") and Great Plains Energy ("GPE"). Transource was formed to compete for and develop transmission projects identified in the post-Order No. 1000 regional planning processes. Transource is currently a member of three regional transmission organizations – PJM, MISO, and SPP. Transource successfully developed and recently placed in service the Iatan-Nashua project in SPP, and is currently developing the Sibley-Nebraska City Project (also in SPP). In addition, Transource is presently developing the Thorofare Creek Area Project in PJM, which was awarded through PJM's sponsorship model competitive process. Transource is an active participant in the ongoing regional planning and competitive developer selection processes in PJM, SPP, MISO, and CAISO.

*Key Points*

Transource commends the Commission for implementing competitive developer reforms in its Order No. 1000 rulemaking. Competition for transmission development opportunities can and will result in significant benefits for consumers. As with any significant policy shift, much can be learned from early experience. As an active, non-incumbent participant in the post-Order No. 1000 competitive solicitation processes in the PJM, MISO, CAISO, and SPP planning regions, Transource has gained perspective on which competitive dynamics are likely to maximize consumer benefits in a manner that is workable for developers, planning regions, and the Commission.

- Based on Transource's experience to date, competitive benefits are maximized in the sponsorship model such as that employed by PJM as compared to the competitive solicitation model through financial bidding. By encouraging developers to tap into their design experience and ingenuity to craft innovative solutions to an identified problem, the sponsorship model fosters a more creative competitive environment that will produce an efficient, 21st century transmission grid.
- While cost estimates and cost containment are among the many factors considered in the sponsorship model, these variables in many instances are the primary deciding factor in competitive solicitation models where the project has already been identified and is subsequently bid on by developers. Such solicitations

become a race to the bottom, with the project oftentimes awarded to the developer proposing the most aggressive cost containment with little to no consideration of the increased risk to project execution. The savings from picking the right project under the sponsorship model are much larger than the savings from picking the cheapest developer for a single project in the bid-based competitive model.

- While cost containment or fixed ATRR bids would seem to benefit consumers, each approach is fraught with challenging issues that may ultimately increase costs to customers.
    - Fixed ATRR bidding is market based and does not result in a cost-based rate, and it is not clear that the current level of competition is sufficient to produce just and reasonable rates. The level of risk undertaken by the developer coupled with the amount of items in transmission project development such as state regulatory approvals and permitting can create instances where customers may be worse off if projects are abandoned or otherwise financially injured for reasons completely out of a developer's control. Lastly, it is unclear how a fixed ATRR would impact the rights of developers and customers under Sections 205 and 206 of the Federal Power Act.
    - Order No. 1000 did not change the regulated nature of transmission as a cost of service business. Cost containment still utilizes the cost of service framework, with developers able to recover the lower of the capped expenditure or their actual cost. But similar to the fixed ATRR project, cost containment shifts risk to investors and is likely to drive up the cost of equity and debt capital and it is not clear whether consumers are left in a better position. The current DCF methodology used to determine ROE does not consider the additional risks of using a fixed ATRR model.
    - Of the two, cost containment seems much more manageable within the current competitive frameworks approved by the Commission under Order No. 1000 compliance filings than by implementing fixed ATRR bidding. Where cost containment is used, the Commission should ensure that the following principles are adhered to:
        - Offering cost containment should be optional for bidders as it may not be appropriate for larger or riskier projects.
        - Developers should be free to cap certain cost components, such as capital costs or O&M, rather than the ATRR for the life of the assets so that developers are not required to hold customers harmless for changes in capital market conditions.
        - Clear rules should be in place for the manner in which costs caps will be evaluated or scored in the competitive developer selection process.
        - Cost containment should not be the primary driver of developer selection but rather a part of a holistic evaluation of developer qualifications, including demonstrated experience and the ability to bring existing infrastructure to operate and maintain the assets.
        - Enforcement of cost containment provisions should be administered by (i) the RTO through the notice and reporting

provisions of the developer selection agreement; and (ii) customers and the Commission under Sections 205 and 206 of the Federal Power Act, including the annual update protocols for developers utilizing formula rates.

In short, Transource believes the sponsorship model offers the best opportunity to harness the benefits of competition for consumers. While cost containment may play a role in parallel with the sponsorship model, it should be among the many factors considered by the planning region. The Commission should continue to explore these and other issues raised by competitive transmission development efforts, and adapt its rate and incentive policies to this new competitive model with guidance and feedback from stakeholders.