Competitive Transmission Development Technical Conference

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Panel 2:
Commission Consideration of Rates That Contain Cost Containment Provisions and Result from Competitive Transmission Development Processes

Introductory Comments of Edward D. Tatum, Jr.
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Thank you for the opportunity to be here today. I am Ed Tatum, and seven months ago I came to American Municipal Power (AMP) to assist in AMP's efforts to address its rapidly escalating transmission costs. The comments I am pleased to offer today are my own and may not reflect the official positons of AMP or its members.

AMP views this conference as part of the Commission's continuing effort to enhance the quality of open access transmission service for the benefit of consumers, and AMP enthusiastically supports that effort. While great progress has already been made, there is still much to be done, and we appreciate the Commission addressing these challenging issues head-on.

By way of background, AMP is a transmission-dependent utility, probably to a greater extent than any other single TDU in the country. AMP owns approximately 1.9 GW's of a fuel diverse generation portfolio, but we depend heavily on open access transmission service over facilities owned by others to deliver the output of our resources to our members. How transmission-dependent is AMP? Well, AMP's 133 members are spread over nine states and 15 different transmission zones in two RTO regions, MISO and PJM. And since AMP's resources meet only about 60% of our members' energy needs, we also depend heavily on the RTO markets. So, in a nutshell, transmission is a huge factor for AMP, and a huge part of its cost structure. To the extent competitive transmission development can help bring down those costs, we are "all in" for that.

Before getting into the details of how cost containment provisions can best be incorporated in rates, I'd like to offer a few general observations that I think bear on the matter at hand.

First, recent history has shown that rate incentives are not really necessary to encourage transmission investment. EEI correctly points out that transmission investment has been on the upswing over the last several years, for a number of reasons having nothing to do with incentives. In fact, what we've seen in recent

years is that a number of companies have pulled money out of merchant generation activities, where their returns were uncertain, and redeployed capital toward their regulated business sectors, especially transmission. The reason is that these companies view FERC-regulated transmission service as providing a stable and relatively attractive return on investment. And while that's all well and good, our concern is that companies not simply pour money into new transmission to reap those rewards for their shareholders. We are interested in getting new transmission built because it is truly needed, not because it provides a richer return than the utilities' other business segments.

Second, no one should view cost containment provisions as a panacea, partly because the strength of the container hasn't really been tested as yet. We know of many, *non-competitive* projects whose final costs wildly exceeded the RTO's original planning estimate – something we feel the Commission ought to think about examining in a separate docket. But for our purposes today, the point is that developers who win a project based in part on a cost containment pledge should be required to live with that cap if the actual costs turn out to be higher than they expected. It sometimes seems to us at AMP that load is made to pony up the difference *whenever* revenues fall short of somebody else's expectations. Let's not let that happen again by relaxing cost containment provisions or allowing excess costs into rates through back-door exceptions to the cap.

Third, because the risk of actual costs exceeding a construction cost cap is real, we should expect that developers will do what they can to hedge the risk. In the end, though, the cost of those hedges eventually will be recovered from consumers. And if a large number of developers build cost containment into their project proposals and factor the related hedging costs into their bids, all boats will rise and the overall cost of transmission for consumers necessarily will go up. Simply put, cost containment provisions aren't a good deal for the consumer if the costs of developers' hedges, or even the impact on developers' borrowing costs, wind up being greater than the construction costs kept out of rates by operation of the cap.

Last, but by no means least – and I feel a bit like a broken record saying this -- the fundamental purpose of the Federal Power Act is to protect consumers. That's not a platitude; it's what the federal courts have said time and again in applying the Act. That purpose would be seriously undermined if the Commission were to adopt a presumption – express or implied -- that the costs of a transmission project selected through a competitive process are "just and reasonable." In practice, such a presumption would effectively shift the burden of proving the justness and reasonableness of rates away from utilities, and impose on consumers the burden of showing that costs are unjust and unreasonable. But, apart from being contrary to the statute, such a presumption relies on the premise that project costs reflect the operation of market forces, and that the costs of

the project selected to be built came out of real head-to-head competition. We have yet to see whether that premise holds any water in real life. As the Commission well knows, we are not yet at the point where it can be said that the planning principles of Orders 890 and 1000 are being implemented with the transparency and process the Commission had in mind in those orders. But, even if they were -- and even if consumers could be certain that a particular project is indeed the most effective solution to a given transmission problem -- there is still not enough experience with the "competitive process" to have confidence that its results are truly competitive. For that reason, a rebuttable presumption that the costs of a project selected through a competitive process are "just and reasonable" relies on a factual predicate that simply hasn't been shown to exist – not yet, and possibly not ever.

Again, I appreciate the opportunity to be here and look forward to the further discussion.