

# FERC ORDER 1000 AND PUBLIC POLICY TRANSMISSION PROJECTS

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## Background

Federal Energy Regulatory Commission (FERC) Order 1000, issued on July 21, 2011, addresses three fundamental reforms affecting transmission planning: regional planning reforms, cost allocation reforms, and non-incumbent developer reforms (Docket No. RM10-23-000). Moving beyond the regional planning provisions in FERC Order 890, the new order requires each public utility transmission provider to consider transmission needs driven by public policy, and expands on interregional coordination requirements. Order 1000 is widely viewed as an opportunity to fund more transmission projects associated with renewable resources. In this paper we provide a high-level summary of FERC Order 1000 as it relates to the issues of public policy benefits and cost allocation.

## FERC's New Six Cost Allocation Principles

In Order 890, FERC outlined nine principles that must be incorporated in the transmission planning process: coordination, openness, transparency, information exchange, comparability, dispute resolution, regional participation, economic planning studies, and cost allocation for new projects (Docket No. RM05-25-000). Order 1000 addresses cost allocation in greater detail. As in Order 890, FERC shied away from a one-size-fits-all approach in Order 1000 and did not take a prescriptive approach with respect to specific cost allocation methodologies. The commission left it to the regional entities to go through an appropriate process involving stakeholders to adopt a cost allocation methodology consistent with the following six principles (Docket No. RM10-23-000, § 586).

1. The costs must be allocated “in a manner that is at least roughly commensurate with estimated benefits.” The benefits include

- reliability, production cost savings, congestion relief, and meeting public policy requirements.
2. “Those that receive no benefit from transmission facilities, either at present or in a likely future scenario, must not be involuntarily allocated the costs of those facilities.”
3. If a benefit threshold is established for determining which projects have net benefits, that threshold should not be higher than 1.25, absent sufficient justification.
4. Costs for regional transmission projects cannot involuntarily be allocated to other transmission regions.
5. The methods for cost allocation, determining benefits, and determining beneficiaries “must be transparent with adequate documentation to allow a stakeholder to determine how they were applied . . .”
6. Different cost allocation methods can be used for different types of transmission projects. For example, the transmission entity has the option, but not the requirement, to establish different cost allocation mechanisms in their tariff for projects designed for reliability versus projects associated with public policy requirements.

## Compliance Requirements for the Public Policy Provision

Utilities and Independent System Operators (ISOs) are in the process of developing filings to meet the October 11, 2012, compliance requirements related to regional planning processes and cost allocation requirements. Most ISOs are in the process of holding stakeholder meetings based upon groundwork laid in Order 890. Stakeholders may want to simplify the compliance filing by applying the cost allocation procedures developed for Order 890 for the new application to public policy projects. However, prior to taking the “simple” path, a number of issues should be considered.

First, while the FERC has shown significant latitude in approving different cost allocation schemes, the common denominator is that there needs to be broad

consensus among the regional participants that the cost allocation process is reasonable. Some regional entities will need to expand the nexus of stakeholders to more broadly encompass the state policymakers and regulators. Second, the beneficiaries of transmission related to public policies such as renewable portfolio standards (RPS) are more likely to be delineated by state boundaries. Third, while Order 1000 requires that costs be allocated commensurate with benefits, the measurement of public benefits is not defined in the order. The process of defining benefits may be controversial. It is not clear that there is regional agreement related to evaluation of public policy benefits.

### **Public Policy Benefit Calculation Issues**

There are a number of high-level issues regarding how to structure the public benefits calculation. These issues include:

- How broad should the definition of a beneficiary be, especially with regard to the determination of who is shielded from the involuntary assignment of costs?
- What is the weight of the cost-benefit analysis in deciding amongst competing projects that all meet the cost-benefit threshold test?
- What is the universe of alternatives that needs to be considered in the assessment of whether a transmission solution is the least-cost approach to achieving the policy?
- How broadly can the future scenarios of likely public policy be defined and does the likelihood need to be part of the calculation of benefits?
- What is the time horizon used to evaluate the associated public policy benefits and should end effects be incorporated into the analysis?
- What is the appropriate discount rate to use and should reliability and public policy benefits have different discount rates?
- How are externalities treated in the calculation?
- How are difficult-to-quantify public costs such as changes in mortality rates for a person or an endangered species measured?

- What is the threshold for no or de minimis benefits to a transmission payer?

How these issues are framed and how the analysis is performed can dramatically alter any results of cost-benefit calculations. Framing the benefits analysis will not start from a blank slate. Federal agencies have dealt with a number of these issues in the analysis of the economic impact of environmental regulations and states have dealt with some of these issues as part of integrated resource planning requirements. The challenge will be in combining these precedents in a manner acceptable to the stakeholders.

### **Public Policy Benefit Calculation Components**

The benefits associated with meeting federal and state environmental regulations and state RPS could potentially incorporate a broad spectrum of issues including:

#### ***Access to Renewable Resources***

A number of transmission project proposals involve connecting remote renewable resource-rich zones with load centers. The net benefits of these projects need to be compared with potential alternatives including construction of renewables closer to load centers, distributed renewable resources, energy efficiency, and reforming electricity pricing. The analysis becomes more complex if it includes externalities such as impact on view corridors, endangered species, critical habitat, human health, and water use issues.

#### **Reduction of Greenhouse Gas Emissions (GHG)**

The complications with GHG emission reductions calculations are associated with the definition of the alternative(s) and value of each lb/ton of reduction. Agreement on what resources are actually being displaced can be complex. The process of comparing the benefits of alternative approaches to transmission, as well as amongst competing transmission projects, will be meaningless if inconsistent valuation assumptions are used.

### ***Lower Air Emissions and Public Health Benefits***

The inclusion of public health benefits that extend beyond what is addressed in U.S. Environmental Protection Agency standards as well as the calculation of those benefits will have to reflect the perspectives of the relevant stakeholders.

### ***Economic Development***

Analyses of the economic value of the green economy and green jobs initiatives have been controversial. An additional complication is identifying the geographic boundaries for calculation.

### ***Fuel Diversification***

The value of the diversification of generation sources can be evaluated in the context of managing volatility in overall electric prices, minimization of shocks from fuel supply issues, and lower costs for a fuel based upon reduced demand (“Valuing Fuel Diversity in Power Markets,” by Graham Shuttleworth and Sean Gammons, NERA Economic Consulting).

### ***Cost Allocation Including Public Policy Benefits***

Several ISOs have FERC-approved cost allocation methodologies that explicitly address projects associated with reliability and market efficiency. The ISOs will need to consider whether these approaches comply with FERC Order 1000 and whether the methodologies are applicable to projects justified based upon public policy. FERC has been silent on the answer to these questions in recent rulings on transmission cost allocation. For example, FERC recently reaffirmed Midwest ISO’s transmission planning process, which includes a new category of transmission projects called “multi-value projects” (MVP) (FERC News Release: Oct. 20, 2011, Docket No. ER10-1791-001). An MVP is defined as a transmission project that is “determined to enable the reliable and economic delivery of energy in support of documented energy policy mandates” or that addresses multiple reliability and/or economic issues affecting multiple transmission zones. The costs of transmission projects that meet the criteria of an MVP

are eligible for 100 percent regional allocation. FERC states that its approval “does not address whether any further modifications may be required in order to comply with the requirements of Order No. 1000.”

In similar fashion, FERC reaffirmed the Southwest Power Pools (SPP) highway/byway cost allocation methodology (Order on Rehearing, issued Oct. 20, 2011, Docket No. ER10-1069-001). Under the highway/byway methodology, costs are allocated to SPP member utilities based on the voltage of a new transmission facility.

Both the Midwest ISO and SPP cost allocation methodologies allocate the costs of “public policy” projects regionwide. And although FERC has not discussed compliance with Order 1000, one indication of FERC’s leaning on this issue may be the following statement from the SPP order: “A strong regionally integrated transmission network provides benefits to all that are interconnected to it.” To the extent that states have different public policies related to renewable resources, there may be new disagreements regarding whether the currently approved cost allocation approaches are consistent with the Order 1000 directive that the cost allocation is commensurate with the benefits.

### ***Summary***

FERC Order 1000 is part of the evolution of reshaping the wholesale power markets. The requirement to include a new class of benefits related to public policy goals in the regional evaluation of transmission projects has the potential to increase the share of renewable generation in the U.S. electricity production mix. We anticipate that there will be significant controversy related to both defining the calculation of public benefits and determining the appropriate cost allocation for transmission projects justified on the basis of public benefits. It will require a significant effort to define how to calculate public policy benefits, determine how those benefits should be allocated among the market

participants, and design the associated cost allocation approach.

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