UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Inquiry Regarding the Commission's Electric Transmission Incentives Policy	)))	Docket No. PL19-3-000

INITIAL COMMENTS OF THE RESALE POWER GROUP OF IOWA

Pursuant to the Notice of Inquiry ("NOI") issued by the Federal Energy Regulatory Commission ("Commission" or "FERC") on March 21, 2019,[1] the Resale Power Group of Iowa ("RPGI") respectfully submits the following initial comments on the scope and implementation of the Commission's transmission incentives regulations and policy and on how the Commission should evaluate future requirements for transmission incentives consistently with Section 219 of the Federal Power Act ("FPA").[2]

INTRODUCTION

In utility rate regulation, no concept is more important than the "just and reasonable" rate. Indeed, the FPA's primary aim and central focus is the protection of consumers from exploitation through excessive rates and charges and unduly discriminatory or preferential practices.[3] Setting a just and reasonable rate is challenging because it requires the resolution of conflicts of economic

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[1] *Inquiry Regarding the Commission's Electric Transmission Incentives Policy,* Notice of Inquiry, 166 FERC ¶61,208 (2019).

[2] 16 U.S.C. §824s.

[3] *Xcel Energy Services, Inc. v. FERC,* 815 F.3d 947, 952 (D.C. Cir. 2016); *NAACP v. FPC,* 520 F. 2d 432, 438 (D.C. Cir. 1975) ("Of the Commission's primary task there is no doubt, however, and that is to guard the consumer from exploitation by non-competitive electric power companies.").

interests among different parties, particularly between investors for whom a rate is a source of income and customers for whom it is an item of expense.[4]

Congress, when amending the FPA to authorize incentives for transmission system improvements, embedded the "just and reasonable" standard (along with its consumer protection purpose and its interest-balancing dynamic) into the new Section 219.[5] The Commission's re-examination of the scope and implementation of its electric transmission incentive regulations and policy must take place against this backdrop with special sensitivity not only by reference to the incentives' effectiveness in performing their intended function, but also to the undesirable side effects the incentives have created.[6] Specifically, the Commission must consider the following factors for each incentive and the incentive policy in general:

- ***Purpose***: What is the incentive/policy's intended purpose? How well does it achieve that purpose?
- ***Effect***: What is the actual effect of the incentive on customers? Has it produced any unintended, adverse side effects? If so, do those consequences outweigh the value created by the incentive?
- ***Balance***: Does the incentive balance investor and consumer interests? If so, how? How well does the incentive accomplish the FPA's aim of protecting consumers from excessive rates?

At the outset of these comments, RPGI wants one point to be very clear: RPGI and its members recognize the importance of transmission system improvements and the role of well-conceived, properly targeted incentives to spur such improvements. Most RPGI members operate

[4] *See also Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) ("[T]he fixing of 'just and reasonable rates' involves the balancing of the investor and the consumer interests.")

[5] 16 U.S.C. §824s(d).

[6] J. Bonbright et al., *PRINCIPLES OF PUBLIC UTILITY RATES* 79 (2d Ed. 1987) (The reasonableness of public utility rates, like the efficacy of prescription drugs, must be evaluated in light of available alternatives, "not only by reference to their effectiveness in the performance of their intended function, but also by reference to the minimization of undesirable side effects.")

in a region of the Midcontinent Independent Systems Operator, Inc. ("MISO") that, prior to 2007, was served by Interstate Power & Light Company ("IP&L") which, like many vertically integrated utilities of the time, did not allocate sufficient funds to updating transmission assets and maintaining long-term system reliability. The need for transmission investment has combined with the nation's increasing reliance on variable, carbon-free generation resources, particularly wind-driven facilities located in northern and western Iowa, to require construction of major transmission lines and other significant capital improvements.

These improvements, however, have come at a high cost. RPGI's members have experienced staggering transmission rate increases that have eliminated any benefit of reduced purchased power costs or congestion relief and have created significant rate disparities among Iowa transmission providers of a magnitude that damages municipal economic development programs and invites bypass. The Commission's transmission incentives have needlessly contributed to, and exacerbated the adverse effects of, these increases. As RPGI will show, these incentives have harmed its members by failing to achieve their purpose, creating adverse (albeit unintended) consequences, and imposing excessive, unjust, and unreasonable rates and charges on customers. For that reason, RPGI respectfully requests that the Commission revise its incentives policy in the manner recommended below.

RPGI appreciates the opportunity to share its perspective on this important matter with the Commission. RPGI will begin with general comments about the Commission's approach to transmission incentives and then will focus specifically on two Return on Equity ("ROE") adders: the adder available to independent transmission providers ("Transco Adder") and the adder for membership in a regional transmission organization ("RTO Adder").

DESCRIPTION OF RPGI

RPGI is a special-purpose governmental entity organized in 1986 pursuant to Iowa law to purchase electric supply, transmission, and related services as an agent for its members. RPGI's members are 24 Iowa municipal utilities, one cooperative, and one privately-owned utility that (with one exception)[7] are exempt from the Commission's jurisdiction under Section 201(f) of the Federal Power Act.[8] A list of RPGI's members is contained in Attachment A. RPGI is legally separate and fiscally independent from other state and local governmental entities.

The electric transmission rates paid by most RPGI members are determined primarily according to the Network Integration Transmission Service ("NITS") Schedule 9 formula rate for ITC Midwest LLC ("ITCM") set forth in Attachment O to MISO's Open Access Transmission Tariff.[9] RPGI's members that do not receive NITS from ITCM purchase that service from MidAmerican Energy Transmission Company ("MidAmerican") at rates that (as discussed below) are a relatively small fraction of ITCM's NITS rates. Other RPGI members located outside MISO are pseudo-tied into MISO where they purchase MISO Schedule 7 Point to Point ("PTP") transmission service.

ITCM's formula rate establishes its annual revenue requirement that is based in part on the application of Commission-approved transmission incentives. Among these incentives are an

[7] The Amana Society Service Company is a small transmission-dependent electric utility that is privately owned by the Amana Society and provides service only to retail customers within the Amana Society in Iowa. Its current annual sales are 96,000 MWh and its peak load is 15 MW. Because of its size, it is not subject to rate regulation by the Iowa Utilities Board.

[8] 16 U.S.C § 824(f).

[9] These members pay ITCM's Zonal rate, which is slightly lower than the ITCM-only NITS rate. The zonal rate is an average rate that is calculated based on a weighted average of the NITS rates of ITCM and five small transmission owners that are in the ITCM Transmission Rate Zone.

RTO Adder of 50 basis points and a Transco Adder of 25 basis points. RPGI has sought review of the Commission's grant of the Transco Adder by the United States Court of Appeals for the D.C. Circuit.[10]

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COMMENTS

A. Approach to Incentive Policy

Question 1: Should the Commission retain the risks and challenges framework for evaluating incentives applications?

Questions about the type of framework the Commission should use for evaluating incentive applications should be resolved only after the Commission defines exactly what it means by "incentive" and makes clear precisely what outcome in today's transmission industry requires

[10] *Resale Power Group v. FERC*, Case No. 16-1088 (D.C. Cir. filed March 4, 2016).

incentives for it to be achieved. The thirteen years since the Commission promulgated its transmission incentive rules have witnessed major changes in planning, financing, constructing, operating, and maintaining transmission systems. Transmission is no longer the undernourished stepchild of the electric industry's generation and distribution sectors. The issue is whether this sea change requires a different approach to transmission incentives. RPGI believes that it does.

1. Characteristics of an Incentive. FPA Section 219 directs the Commission to establish, by rule, "incentive-based (including performance based) rate treatments for the transmission of electric energy. . .for the purpose of benefitting consumers by ensuring reliability and reducing the cost of delivered power by reducing transmission congestion."[11] Neither Section 219 nor the Energy Policy Act of 2005 defines "incentive." To interpret Congress's intent in Section 219(a), it is appropriate to rely on the word's plain meaning.[12] Thus, an incentive is "a payment or concession to stimulate greater output or investment."[13] An incentive is not a reward or bonus for doing something one has accomplished or is already doing.[14] Rather, by definition, it is an encouragement designed to produce a result that would not otherwise have occurred.

An incentive therefore requires a pre-existing need. Under regulatory statutes like the FPA, adding cost to a customer's bill cannot be justified initially or continued in effect unless it meets a need that cannot be met economically or efficiently in any other way. An incentive must be limited in time or, if it is permanent, it must regularly produce new ongoing actual benefits to customers

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[11] FPA Section 219(a).

[12] *Federal Energy Reg. Comm'n v. Martin Exploration Management Co.*, 486 U.S. 204, 209-10 (1988) (quoting *Bethesda Hospital Ass'n v. Bowen*, 485 U.S. 399, 403 (1988) ("The plain meaning of the statute decides the issue presented.")).

[13] "Incentive," Oxford Dictionaries. Oxford University Press. http://www.oxforddictionaries.com/us/definition/american_english/incentive (accessed June 24, 2019).

[14] *Policy Statement on Incentive Regulation*, 61 F.E.R.C. ¶61,168 at P 61,589-90 (1992).

that significantly outweigh its adverse direct and indirect impacts. As the Commission has stated, incentives cannot reward past behavior because doing so would "violate the objective of benefitting customers."[15] Stated differently, an incentive cannot be used to encourage behavior that has been completed.[16] Perhaps Commissioner Brownell said it best in her concurring opinion in *Trans-Elect, Inc.*: "I am not going to ask customers to pay more for the same old product they are receiving today. Increasing costs to customers should be linked to *demonstrable improvements* in quantity and quality of service."[17]

Order No. 679 echoes this principle. The Commission stated that it would not authorize incentives that only serve to increase rates without providing "any *real incentives* to construct new transmission infrastructure."[18] Quoting the language from FPA Section 219(a) cited above, the Commission stated that the very purpose of its incentive rules is "to benefit customers by providing *real* incentives to encourage *new* infrastructure, not simply increasing rates in a manner that has no correlation to encourage *new* investment."[19] The Commission emphasized that it would not grant an incentive as a "bonus for good behavior," but would apply incentives on the basis of an application's merit.[20]

A real incentive therefore requires an action beyond what is normally required or expected or a benefit greater than mere satisfaction of a given standard. Embedded in a healthy, effective incentive regime is dynamism. As the incentive accomplishes its purpose, it defines a "new

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[15] *Id.* (emphasis added).

[16] *New England Power Pool*, 97 F.E.R.C. ¶61,093 at P 61,480 (2001).

[17] *Trans-Elect, Inc.*, 98 F.E.R.C. ¶61,368, at P 62,596 (2002) (emphasis added).

[18] *Promoting Transmission Investment through Pricing Reform*, Order No. 679, 116 FERC ¶61,057 at P 6 (2006) (emphasis added).

[19] *Id.* (emphasis added).

[20] *Id.* at P 26.

normal" that either obviates its need entirely or requires its retooling to spur achievement of a higher or different objective.

2. What outcome does the Commission's current rules incentivize? As currently structured, the Commission's incentive regime encourages a transmission provider to undertake large-scale, high-dollar projects to maximize the value of its rate base. In ITCM's case, a combination of favorable rate treatments has resulted in an astonishingly high level of rate base additions. Since its formation in 2007, ITCM has financed and constructed improvements that dramatically increased its gross plant in service. For its first year of operations, ITCM rates were those charged by IP&L (the utility that sold ITCM its transmission assets), which were based on 2006 data. In its 2009 MISO Attachment O formula rate filing, ITCM valued its Total Gross Transmission Plant at $878.05 million.[21] The same item in its 2019 filing was $3,628.67 million – a 10-year increase of over 313% ($2,750.62 million). ITCM outpaced all other MISO-North and Central transmission owners in this respect.

Those same filings show that ITCM's projected rate base has grown by over $2,135.44 million, from $581.19 million to $2,716.63 million – an increase of over 367% since 2009. No other transmission owner in the MISO North and Central regions has come close to matching ITCM's percentage increases in rate base investment. In terms of encouraging rate base additions, it appears that the incentives granted by the Commission to ITCM, when combined, have achieved their purpose.

3. Transmission Rate Increases. The apparent success of the Commission's incentives has been purchased at a very high cost. ITCM's acquisition of IP&L's transmission

[21] The data used in these comments regarding year-to-year changes in ITCM's gross plant in service, rate base, and transmission service rates are drawn from the formula rates contained in Attachment O forms filed by ITCM in January of each year.

system was completed in December 2007. As of January 2008, the monthly NITS rates for the newly transferred IPL transmission system was $2.577/kW-month. As ITCM invested in transmission infrastructure, its ITCM zonal NITS rates climbed annually at a compound rate of 12.79%. Currently, MISO's ITCM zonal NITS rate stands at $9.685/kW-month - a 276% cumulative rate increase since 2008. No other transmission owner in MISO's North and Central regions has had its NITS price increase at a rate anything close to this magnitude over this period.

In contrast, MISO's rate for Point-to-Point Through and Out Transmission Service ("PTP Service") has only modestly increased since 2008. Unlike the NITS rate, this rate is calculated based on dividing the aggregate MISO Attachment O revenue requirements for all MISO transmission owners by the total MISO billing demand in kWs, thereby producing a MISO average transmission rate. In 2008, the PTP Service rate was $2.112/kW month. Over the past eleven years, it has increased at a compound rate of 4.00% per annum. Currently, the rate is $3.251/kW month for a total increase of 53.93% over 2008 levels – a far cry from the 276% increase for the ITCM zonal NITS rate.

ITCM's NITS rates for 2019 are the highest in the MISO North and Central regions and over 30% higher than the NITS rate charged by Dairyland Power Cooperative ($7.430/kW month), which occupies the number two ranking. More importantly for the purposes of this proceeding, ITCM's current NITS rate is over ***4.4 times*** the NITS rate charged by MidAmerican ($2.201/kW). ITCM's NITS rate is likely to go even higher as it continues to make significant transmission infrastructure investments.

From 2008 to 2019, ITCM's NITS rates comprised an increasing percentage of RPGI's total wholesale electric power costs. In 2009, charges for ITCM zonal NITS and ancillary services constituted 17.80% of RPGI's total wholesale power costs on the ITCM system. By 2018, this percentage had increased to nearly 41%. With steady to falling MISO energy prices and continued ITCM transmission improvements, ITCM zonal NITS and ancillary services in 2019 and 2020 are expected to increase as a percentage of wholesale power costs on the ITCM system.

3. Policy Consequences. The path of public policymaking is strewn with the remains of good intentions felled by unintended consequences. The Commission's current approach to transmission incentives has accomplished rapid renewal of the transmission grid but has exacted a very high cost and produced adverse consequences that harm customers and cut against the Commission's policy objectives. The experience of RPGI's members illustrates these negative effects.

(a) ***Impairment of Economic Development.*** Municipal utilities in Iowa operate in an intensely competitive environment where even small differences in delivered power supply costs can have significant adverse consequences on RPGI members and other municipal consumers. These consequences are especially disadvantageous for municipal economic development initiatives.

With 183 retail electric utilities operating in the state, there are many locations where an alternative electric service provider with a lower delivered cost of electricity can be found near a municipal utility's service area – sometimes just across the street. A municipal utility that receives NITS from ITCM will have higher retail rates due to transmission charges than one served by another MISO Transmission Owner or a transmission provider that is not part of MISO.

Retail electric rates are a major factor in a community's economic development efforts. A prospective customer is generally unconcerned with the cost of individual service components (generation, transmission, distribution) that comprise overall electric rates. The customer's primary concern is normally centered on one utility's delivered cost of electricity per kilowatt hour versus another. Consequently, if a community's municipal utility charges its customers a higher electric service rate than its competitors, local officials will frequently pressure the municipal utility to identify aggressive ways to lower the community's retail electric rates to levels that are equal to, or lower than, its competitors' rates. Often, even a very small difference in electric service rates can be a major factor in a prospective customer's decision about where to locate its new business. It can also be a major factor in a current customer's decision of whether to remain in, or move out of, a community.

The City of Mount Pleasant, Iowa is a good example of this dynamic. The Mount Pleasant Municipal Utilities department ("MPMU") serves approximately 4,200 electric customers. Its service territory is surrounded geographically by the service territory of Access Energy, a distribution member-owned cooperative. MPMU's power supply is delivered from the MISO system by means of a two-mile 69 kV transmission line owned and operated by the Northeast Missouri Electric Power Cooperative ("NEMO"), a generation and transmission cooperative of which Access Energy is a member. NEMO is not a member of MISO. MPMU pays the NEMO NITS rate for this service. MPMU's load and generation are pseudo-tied into the MISO transmission system and MPMU, through RPGI, pays MISO PTP transmission rates.

Prior to 2014, MPMU received NITS from ITCM in addition to the NEMO NITS which caused its delivered cost of electricity to be significantly higher than the price of electric service charged by many other Iowa municipal utilities and cooperatives. MPMU's high electric price became a major competitive disadvantage in Mount Pleasant's economic development efforts, so much so that city officials requested MPMU to investigate ways to reduce its electric service rates.

Beginning on January 1, 2014, MPMU continued purchasing power supply in MISO under the same interconnection arrangements but discontinued use of the ITCM zonal NITS rate and qualified for MISO's PTP Service rate, which, as previously noted, is substantially lower than ITCM's zonal NITS rate. With this change, MPMU avoided ITCM's zonal NITS rates and reduced its annual transmission delivery costs by a net of approximately $920,000 while continuing to pay the NEMO NITS rates. This reduction, in turn, has lowered MPMU's electric purchase cost by 1.172 cents per kWh, thereby enhancing its competitive position.

(b) ***System Bypass.*** Other RPGI members have sought to reduce their price for delivered electricity by bypassing ITCM's system altogether. For example, the city of La Porte City, Iowa is building its own 12.5-mile, 69 kV line to interconnect with MidAmerican's transmission system for a cost of $2 million. This new line will cut its transmission costs by about $250,000 annually (25.7% of its total annual electric costs) by allowing the city to shift from ITCM to MidAmerican NITS rates. Debt service on the new line will offset a significant part of these savings, but the city nevertheless is expected to see immediate financial benefits of this shift away from ITCM's zonal NITS rates.

The cities of Dike and Stanhope, Iowa also left ITCM's system. When ITCM acquired IP&L's transmission system in 2007, IP&L retained ownership of the 34.5 kV substations that served each of these cities and charged both cities a Facilities Charge for that service. When ITCM replaced the 34.5 kV transmission lines connected to these substations with 69 kV lines, IP&L upgraded the substations, which caused the Facility Charge to increase by 370% for Dike and 814% for Stanhope. These increases, combined with ITCM's much higher NITS charge, forced both municipal utilities to leave ITCM's system at the end of 2013 to obtain lower cost transmission service from other sources outside MISO.[22]

[22] Dike is now served by Grundy County Rural Electric Cooperative and Corn Belt (non-MISO). Stanhope is served by Heartland Consumers Power District.

In 2012, the City of Whittemore, Iowa's electric utility was forced to find an alternative to its existing transmission interconnection when ITCM announced it would be retiring its 34.5 kV transmission line that interconnected with the city's system. As the city investigated its options for continuing to receive NITS from ITCM, none of the ITCM-based options proved to be cost effective given the combination of ITCM's high zonal NITS rates and the costs of constructing a new transmission line and facilities. Ultimately, the city decided to build a new substation and a feeder line to interconnect with Corn Belt Power Cooperative (Corn Belt"), a transmission cooperative that is a member of the Southwest Power Pool ("SPP"), not MISO. Ultimately, Whittemore was pseudo-tied from SPP into MISO, thereby enabling it to use MISO's PTP Service over MISO's system. The savings produced by the difference between ITCM's high NITS rates and the much lower MISO PTP rates have funded the transmission line to interconnect with Corn Belt.

Loss of electric load harms both the transmission owner's remaining customers and attainment of the Commission's policy objectives. First, departure of customers causes a high-cost transmission provider to spread its revenue requirement over a smaller load, which further exacerbates the negative effect of the high transmission rates described above. For some municipalities, higher rates may make previously uneconomic bypass options financially viable, which could lead to additional load loss and even higher rates. For other municipalities that do not have a realistic option to bypass a high-cost transmission system, higher rates place them at a distinct disadvantage that is not easily mitigated.

Second, forcing municipalities to utilize their debt capacity to build otherwise unnecessary transmission facilities to bypass a high-cost transmission provider may cause the municipality to postpone, or even forego, other system improvements that would update and enhance their distribution systems. When seeking to update the nation's electric infrastructure, it is not enough to focus on the transmission system. Local distribution infrastructure also requires updating and improvement. RPGI recognizes that the Commission does not regulate distribution systems, but the Commission nevertheless must realize that at least for some wholesale customers, its incentive policies may unnecessarily divert capital resources from other necessary distribution infrastructure renewal. Although municipalities are well-acquainted with the difficulties of balancing limited financial resources against long lists of infrastructure needs, the imposition of costs to construct otherwise unnecessary facilities to bypass a high-cost transmission system with rates made uneconomic solely by the rapid addition of transmission infrastructure over-stimulated by the Commission's incentives, places an undue burden on municipalities and their customers.

Finally, a policy that results, as it has in Iowa, in high differentials among the NITS rates for transmission providers, distorts the Commission's vision of a highly competitive wholesale power market where power moves over the grid to ensure that "electricity consumers pay the lowest price possible for reliable electric service."[23] When transmission costs rise dramatically for one transmission provider (as they have for ITCM), they can wipe out any savings in power supply costs for customers of that system and create the type of economic distortions that cut against the Commission's transmission initiatives.

(c) ***Summary***. Rate increases and unintended consequences have decidedly skewed *Hope's* customer/investor balance of interests with regard to transmission rates. The goal of a renewed transmission system is critical, but it cannot be purchased by sacrificing the FPA's consumer protections. By requiring incentivized rates to be "just and reasonable," Congress

[23] *Final Rule on Regional Transmission Organizations*, Order No. 2000, 89 F.E.R. C. ¶61,285 (1999), 1999 FERC LEXIS 2692 at **4.

intended transmission infrastructure renewal to occur in a manner, at a pace, and with a cost that would benefit, not punish, customers. At least for RPGI's members, whose delivered cost of electricity has skyrocketed since 2008, the Commission's portfolio of incentives has not fulfilled Congress's intent.

Thus, before becoming mired in the details of whether an incentive should be approached on a risk/challenges, project benefits, or project characteristics basis, RPGI urges the Commission to recognize the importance of taking customer rate impact into account. It is at the heart of the Commission's overall mission and must be the basis on which all incentive-related policy choices must be weighed.

In its remaining comments, RPGI will address ways in which the Commission can revise its incentives to better align investor and customer interests and, going forward, fix the current imbalance.

B. Existing Incentives

1. Transmission-Only Companies

Question 57: Does the Transco business model continue to provide sufficient benefits to merit transmission incentives? What information should an entity seeking a Transco incentive provide to demonstrate sufficient benefits?

In RPGI's view, the Transco business model has never produced benefits sufficient to merit favorable rate treatment over other corporate forms. But even if it did, the maturing of organized markets and the RTO/ISO management of, and planning for, regional transmission systems have taken away any rationale for Transcos' continuing preference. RPGI recommends that the Transco Adder be discontinued.

(a) ***The Commission's Transco Preference.*** For nearly twenty years, the Commission has favored Transcos, which it defines as stand-alone transmission companies that have been approved by the Commission and sell "transmission services at wholesale and/or on an unbundled retail basis, regardless of whether it is affiliated with another public utility."[24] The Commission's preference for Transcos finds its clearest expression in the Transco Adder, although the Commission regularly has granted Transcos a number of other incentives.

The Transco Adder's purpose is to provide Transcos an ROE that "both encourages Transco formation and is sufficient to attract investment after the Transco is formed."[25] The Commission's decision to grant this incentive was based on the "proven and encouraging" track record of Transco investment in transmission infrastructure – a record it believed was related to the standalone nature of these entities.[26] According to the Commission, Transcos would utilize their additional return for capital spending, a conclusion based on the fact that at the time of Order No. 679's issuance, Transcos were "spending capital aggressively, reinvesting any earned returns and spending a significant amount more than they are earning."[27]

The concept of incentivizing Transco formation did not begin with Order No. 679, but rather with the Commission's efforts to establish competitive wholesale power markets in the mid-1990s and early 2000s. The Commission's experience in these efforts undergirded and informed Order No. 679's approach.

In 1996, the Commission issued Order Nos. 888 and 889, which mandated non-discriminatory open access transmission services by public utilities and promulgated stranded cost recovery rules that, in the Commission's view, would "provide a fair transition to competitive

[24] 18 C.F.R. §35.35(b) (2019).

[25] Order No. 679, 116 FERC ¶61,057 at P 221.

[26] *Id*. at PP 222 and 224.

[27] *Id.* at P 226.

markets."[28] The Commission discovered, however, that "traditional management of the transmission grid by vertically integrated electric utilities was inadequate to support the efficient and reliable operation that is needed for the continued development of competitive electricity markets" and that continued discrimination in the provision of transmission services by vertically integrated utilities was also impeding that development.[29] Therefore, on December 31, 1999, the Commission issued Order No. 2000 to advance the formation of RTOs. According to the Commission, the creation of independent regionally operated transmission grids would promote competition, which it considered "the best way to protect the public interest and ensure that electricity consumers pay the lowest price possible for reliable service."[30]

Central to the Commission's efforts to establish effective and efficient RTOs was the feasibility and vitality of the stand-alone transmission business model.[31] According to the Commission, "the principle of independence is the bedrock upon which the ISO must be built" and that "this principle must apply to all RTOs, Transcos or variants of the two."[32] Transmission-only companies, as opposed to vertically integrated utilities, however, were new and unproven entities. The Commission did not know how financial markets would view the risk associated with these companies.[33]

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[28] Order No. 2000, 1999 FERC LEXIS 2692 (Part 1) at **12.

[29] *Id*. at **4.

[30] *Id*.

[31] Order No. 2000, 1999 FERC LEXIS 2692 (Part 5) at **7.

[32] Order No. 2000, 1999 FERC LEXIS 2692 (Part 1) at **199-200.

[33] Order No. 2000, 1999 FERC LEXIS 2692 (Part 5) at **82 ("[S]ome commenters assert that stand-alone transmission companies (e.g. Transcos) are risker because they have a less-diversified portfolio of assets than a vertically integrated utility. Other commenters argue that participation in an RTO that is an ISO is inherently riskier, suggesting that increased risk comes from ownership of transmission assets that are ceded for purposes of operational control to another, non-affiliated utility.").

Accordingly, the Commission stated that it was willing to allow higher rates of return to compensate investors for that risk, justifying the higher transmission costs because it viewed transmission as having a minimal impact on the overall price of delivered electricity. The Commission stated that "*[S]ince the costs of transmission are a small portion of total electric costs*, getting transmission pricing right means that the industry will be able to capture significant benefits from promoting competitive generation markets."[34] The Commission cited the comments of Salomon Smith Barney, which noted that "the direct total costs of transmission service represents about six to seven percent of the average customer's bill, and raising transmission prices even as high as 25 percent in order to attract capital adds only two percent to the overall electric bill."[35]

Order No. 2000 focused on the establishment of independent regional RTOs and so the Commission couched its discussion of the Transco model in terms of RTO structuring.[36] The Commission later extended eligibility to Order No. 2000's innovative rate treatments to an independent, stand-alone transmission company that intended to join an RTO.[37]

Order No. 2000 contemplated that RTOs would be operating across the nation by December 31, 2001, but by early 2003, only two RTOs (MISO and PJM Interconnection, Inc.) and only one Transco had reached that milestone. Having approved incentives for both RTOs and Transcos in a few individual cases,[38] the Commission decided it was necessary to adopt an

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[34] *Id*. at **14.

[35] *Id*. at **83 fn, 653.

[36] *See e.g.* Order No. 2000, 1999 FERC LEXIS 2692 (Part 1) at **161.

[37] *International Transmission Co.*, 92 FERC ¶61,276 (2000).

[38] *See, e.g. Trans-Elect, Inc.*, 98 FERC ¶61,142 (2002); *Midwest Independent Transmission System Operator, Inc.*, 100 FERC ¶61,292 (2002); *Removing Obstacles to Increased Electric Generation and Natural Gas Supply in the Western United States*, 94 FERC ¶61,277 (2001).

incentive policy to spur RTO and Transco development.[39] Among the incentives approved by the Commission was a form of the Transco Adder. Transcos that participated in RTOs and met certain independent ownership requirements would qualify for an incentive equivalent to 150 basis points applied to the book value of facilities at the time of their divestiture from a vertically integrated utility. The lump sum would be determined at the time of divestiture but would be amortized and recovered over the period during which the incentive was applied. According to the Commission, recovery of the lump sum dollar amount would "yield the same amount, after taxes, of the increase in after-tax returns resulting from application of the ROE adder to current rate base over the period during which the incentive is applied."[40]

Shortly after issuing the 2003 Pricing Policy, the Commission approved a Transco Adder of 100 basis points and a 60/40 equity/debt capital structure for International Transmission Company ("ITC"), a Transco created by DTE Energy's divestiture of its transmission assets.[41] After analyzing ITC's ownership and governance structure to assure the presence of measures to prevent market participants' participation in ITC's decision-making, the Commission, noting that independent operation of transmission assets was an important policy objective, warned that "[w]hile this transaction is afforded the use of two ratemaking tools discussed in the proposed policy statement, we do not intend for this to be the case for future transactions."[42] ITC Holdings, Inc. (ITC's corporate parent) subsequently became the only publicly-traded, stand-alone transmission company in the United States.

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[39] *Proposed Pricing Policy for Efficient Operation and Expansion of Transmission Grid*, 102 FERC ¶61,032 at P 20 (2003) ("*2003 Pricing Policy Statement*").

[40] *Id.* at P 25.

[41] *ITC Holdings Corp.*, 102 FERC ¶61,162 (2003).

[42] *Id.* at P 68.

The *2003 Pricing Policy Statement* was superseded by the enactment of Section 219 and the Commission's issuance of a Notice of Proposed Rulemaking to promulgate the incentive rules mandated by that provision.[43] This notice led to the issuance of Order No. 679 and its progeny and the Commission's approval of several Transco Adders for new Transcos. Throughout this process, the Commission affirmed its belief in the unique efficacy of the Transco business model, stating that "Transcos' for-profit nature, combined with a transmission-only business model, enhances asset management and access to capital markets and provides greater incentives to develop innovative services."[44]

The question immediately arose whether "independence" meant complete, stand-alone independence from market participants or some lesser degree of separation. In Order No. 679, the Commission stated that while independence was an "important component of the positive contribution of Transcos on investment in needed infrastructure," a Transco with active ownership by a market participant would be eligible for the Transco incentives "to the extent it can show. . . why active ownership by an affiliate does not affect the integrity of its investment planning, capital formation, and investment processes or how its business structure provides support for transmission investments in a way similar to the structure of non-affiliated Transcos or Transcos with only passive ownership by market participants."[45] The Commission refused to establish a precise formula or method for correlating the degree of a Transco's independence with the amount of the Transco Adder, preferring to evaluate each case on its merits.[46] The Commission noted that

[43] *Promoting Transmission Investment through Pricing*, 113 FERC ¶61,182 at P 2 fn 7 (2005).

[44] *New York Regional Interconnection, Inc.*, 124 FERC ¶61,259 at 41 (2008); *Star IO, L.L.C.*, 122 FERC ¶61,306 at P 19 (2008). *See also Green Polar Express LP*, 127 FERC ¶61,031 at P 86 (2009)

[45] Order No. 679, 116 FERC ¶61,057 at P 240.

[46] *Id.* at P 239.

the three then-existing Transcos, which had significantly increased their transmission investment post-formation, were either totally independent of market participants or could meet the independence standards of the Commission's Policy Statement Regarding Evaluation of Independent Ownership.[47]

As the years passed, the Commission granted Transco Adders and other incentives to both single project Transcos and to Transcos that owned extensive transmission systems.[48] Transco Adders ranged from 25 to 100 basis points depending on a Transco's degree of independence and other factors. The Commission never wavered from its confidence in the Transco business model's unique efficacy to accomplish the goal of transmission infrastructure renewal even though many of its fundamental assumptions regarding the model have not been borne out in practice.

(b) ***The Commission's Transco Preference is Outdated*.** The Commission's preference for the Transco business model is outdated. The preference was born at a time when vertically integrated utilities were impeding the transition to fully competitive electric power markets by failing to make necessary investments in their transmission infrastructure and were favoring their own generation assets over those of independent power producers. rom the Commission's standpoint, independence from the traditional utility structure was a desirable characteristic for breaking through institutional inertia and attaining a critical policy objective.

Nearly twenty years later, huge strides have been made to achieving the Commission's objective. Nine RTOs and Independent System Operators serve over two-thirds of electric

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[47] Order No. 679, 116 FERC ¶61,057 at P 240. The referenced policy statement was issued by the Commission in 2005 to establish a non-exclusive list of considerations it would consider in evaluating an independent transmission company's ownership structure. *18 CFR Part 35 Policy Statement Regarding Evaluation of Independent Ownership and Operation of Transmission*, 111 FERC ¶61,473 (2005).

[48] *See, e.g.*, *GridLiance West Transco LLC*, 164 FERC ¶61,049 (2018); *Atlantic Grid Operations A LLC*, 135 FERC ¶61,144 (2011); *Primary Power, LLC*, 131 FERC ¶61,015 (2010).

consumers in the United States and Canada.[49] Power producers compete vigorously for wholesale customers and claims of utilities favoring their own production have diminished as congestion has been reduced and as independent entities monitor grid traffic. In MISO, planning is occurring on a regional basis, with new, multi-value transmission projects being constructed across utility systems and state lines. In short, today's transmission grid operates at an unprecedented degree of integration according to a uniform set of reliability standards established by the National Electric Reliability Council – an achievement that twenty years ago was little more than words on paper.

Thus, if, as the Commission believed, Transcos were a lynchpin in its restructuring process, the purpose for encouraging their formation has been fulfilled. The Commission's Transco preference should be discontinued.

(c) ***Accelerated Transmission Infrastructure Investment Has Not Depended on a Transmission Provider's Business Structure***. As previously noted, the Commission's Transco preference was based on the "proven and encouraging" track record of Transco investment in transmission infrastructure – a record it believed was related to the standalone nature of these entities. The past twenty years, however, have shown that the willingness to invest in grid improvements is not limited to Transcos in a degree that justifies the Transco preference.

Since MISO's designation as an RTO in 2003, over $19 billion in transmission system improvements have been completed.[50] Transcos have played a significant, but not exclusive, role in these projects. In fact, out of MISO's fifty-one transmission owner members, only eight members appear to qualify as Transcos,[51] three of which are wholly-owned subsidiaries of ITC

[49] *ISO/RTO Council History*, available at https://isorto.org/#about-section (last viewed June 24, 2019).

[50] https://www.misoenergy.org/about/media-center/miso-approves-2018-transmission-plan/ (last viewed June 24, 2019).

[51] https://cdn.misoenergy.org/Current%20Members%20by%20Sector95902.pdf (last viewed June 24 2019). These Transcos are AEP Indiana Michigan Transmission Company, Inc; Ameren Transmission

Holdings, Inc.[52] Focusing for the purpose of these comments on MISO Transmission Expansion Projects ("MTEP"), approximately $1.951 billion out of the $3.48 billion cost of MTEP Baseline Reliability, Generation Interconnection, and Market Efficiency Projects from 2006 through 2016 was allocated to the pricing zones for five Transcos, meaning that these Transcos were allocated the cost of, and presumably completed, projects representing 55% of this cost, leaving the other 45% to be allocated to, and presumably completed by, other entities.[53] Regardless of the exact percentages, at least in MISO, Transcos have not been such a singular source of new transmission investment as to qualify them for any business structure preference.

(d) ***The Transco Preference has not produced standalone transmission companies and, in fact, has operated against that objective.*** The Commission began granting preferential rate treatment to Transcos as an incentive for the formation of stand-alone, transmission-focused companies that would focus on investment in new infrastructure. Several Transcos were formed and were awarded incentives, both before and after Order No. 679. In MISO, however, only one group of companies – ITC Holdings and its subsidiaries - was formed that did not have ties to market participants. ITC Holdings included in its founding documents certain prohibitions on stock ownership in market participants by officers and directors as well as other protections for

Company of Illinois; American Transmission Company; International Transmission Company (d/b/a ITC Transmission); ITC Midwest LLC; Michigan Electric Transmission Company, LLC; Pioneer Transmission, LLC; and Prairie Power, Inc. The Commission has approved a formula rate for an additional Transco, GridLiance Heartland LLC, but as of January 29, 2019, it did not own any transmission assets in MISO. *GridLiance Heartland LLC*, 166 FERC ¶61,067 (2019).

[52] International Transmission Company, ITC Midwest LLC, and Michigan Electric Transmission Company.

[53] See *MISO Transmission Expansion Plan 2017*, Appendix A-2.2, Indicative MTEP06 through MTEP16 Cost Allocation Summary for Baseline Reliability, Generation Interconnection, and Market Efficiency Projects," available at https://www.misoenergy.org/planning/planning-test/mtep-2017/#t=10&p=0&s=FileName&sd=desc. RPGI recognizes that these projects represent only a portion of the $19 billion in projects as being completed in MISO since 2003, but these projects provide a strong indication of the commitment of non-Transcos to improvement of MISO's transmission system.

independence. ITC Holdings became enormously successful, so much so that in 2016, the company's management was able to declare to shareholders that "[o]ur total shareholder return has outperformed the Dow Jones Utility Index every year since our initial public offering in July 2005 and we have produced a total shareholder return over that period of over 554%."[54]

But business success attracts corporate suitors. By the time its management made this statement, ITC Holdings had announced its acquisition by Fortis Inc. and GIC Private Ltd. With this transaction, which was consummated on October 14, 2016,[55] ITC Holdings' operating companies lost their standalone character and, as the Commission recognized last fall, a substantial quantum of their independence.[56] If the Commission's preference for Transcos was meant to encourage the formation and continued operation of truly independent, standalone Transcos, it utterly failed.

(e) ***Transcos have not necessarily invested the extra capital produced by the Commission's Transco preference in new transmission infrastructure.*** According to the Commission, Transcos deserve preferential rate treatment because they utilize their additional return for capital spending. What might have been the case fifteen years ago is not the case now. With low interest rates in place, Transcos have relied heavily on debt to fund transmission capital improvements.[57] This is particularly true for Transcos like ITC Holdings, which is leveraging the

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[54] ITC Holdings, Inc., Schedule 14A, *Proxy Statement Pursuant to Section 14)a of the Securities Exchange Act of 1934*, dated April 8, 2016 at p. 20.

[55] *Fortis, Inc.*, Docket No. EC16-110-000, Notice of Consummation, FERC Acquisition No. 20161024-5034 (filed October 24, 2016).

[56] *Consumers Energy Co. v. International Transmission Co.*, 165 FERC ¶61.021 at P 68 (2018).

[57] For example, as of December 31, 2018, ITC Holdings and its affiliates had issued over $9.1 billion in corporate bonds and notes. *See* ITC Holdings Corp., 2018 Form 10-K available at https://www.itc-holdings.com/docs/default-source/sec-filings/itc-2018-12-31-10k-final.pdf?sfvrsn=7e7fcaf6_2 (last viewed June 24, 2019).

difference between its capital structure (40% equity/60% debt) and the capital structure of its operating companies (60% equity/40% debt) to enhance its returns.

(f) ***Conclusion***. The Commission's reasons for promoting the Transco business model above other business forms either have proved to be inaccurate or unsupported by experience. The Transco business model no longer requires or deserves the special rate treatment that the Commission has granted.

Question 58: Should the Transco incentive remain available to Transcos that are affiliated with a market participant? If so, how should the Commission evaluate whether a Transco is sufficiently independent to merit an incentive?

The Transco incentives should not remain available – period. As previously noted, the Transco business model itself does not justify any special rate treatment or preference above other business structures. Even if such preference were justified, however, the combination of incentives can produce unintended adverse consequences for customers that can subvert the policy objectives sought by Section 219 and the Commission's rules. The Transco Adder in particular is not an effective or necessary tool for accomplishing these objectives.

(a) The stacking of Transco incentives can prevent customers from realizing the savings produced by competitive power markets and the advent of renewable energy resources. Fundamental to the development of the Commission's policy of incentivizing the Transco's construction of new transmission infrastructure was its belief that significant additional costs associated with Transcos would continue to constitute a relatively minor portion of the total cost of delivered electricity. When the Commission issued Order No. 2000, transmission costs represented only 6% to 7% of the average customer's electric bill so the Commission felt comfortable that even a 25% increase in transmission costs would add only 2% to the total bill.[58]

The Commission continued to hold this belief as it adopted incentives intended to stimulate new construction. In the order that approved the sale of IP&L's assets to ITCM and authorized certain Transco rate incentives (but not the Transco Adder, as discussed below), ITCM, echoing the Commission, countered concerns raised by a coalition of municipal utilities about the transaction's possible adverse rate effects by arguing that "even a 20 percent increase in transmission costs . . . would translate into only a two percent increase in the total cost of electricity. That amount likely will be more than offset by savings from reduced congestion, access to lower cost power, and other benefits. . . ."[59] The Commission agreed and approved the transaction, stating that while the proposed sale would have rate effects, the creation of an independent, standalone transmission company can "result in significant benefits for customers that can outweigh any rate effect a transaction would create."[60]

It has not happened that way, at least in RPGI's experience. As noted above, transmission costs have become a high percentage of its members' total electric costs. Members relying on ITCM zonal NITS service have seen their electric transmission rates increase by 276% since 2008, with almost all of that increase attributable to higher transmission investments. In 2019, transmission costs represent approximately 41% of total electric costs – an amount that has eliminated any benefits of lower cost power supplies. At least for RPGI, the Commission's policy of promoting improved transmission infrastructure by granting Transco incentives has resulted in

[58] Order No. 2000, 1999 FERC LEXIS 2692 (Part 1) at **83 fn. 653.

[59] *ITC Holdings*, 121 FERC at P 117 (emphasis added).

[60] *Id.* at P 128 (footnote omitted).

capital investments being made at such an overwhelming level and at such a dizzying pace that those RPGI members in rough geographic proximity to lower transmission-rate systems have abandoned, or are in the process of abandoning, ITCM where possible, as previously discussed.

Perhaps the Commission's Transco incentives themselves have worked too well or perhaps the Commission's stacking of multiple incentives has combined with historically low interest rates to drive transmission capital spending to a historic high. Whatever the case, for RPGI members, rate increases attributable to transmission improvements have reached intolerable levels, are working against attainment of the Commission's policy objectives, and are violating Section 219's mandate that even incentivized rates must be just and reasonable. As a result, the Commission should not grant Transco incentives of any kind.

(b) ***Independence from market participants is nothing more than a convenient fiction for affiliated Transcos*****.** If the Commission decides to continue awarding Transco incentives, especially the Transco Adder, it should not determine that award based on the Transco's independence from market participants. The only truly independent Transco is one that stands alone without any ties whatsoever to such participants. But as the Commission discovered, Transcos completely unaffiliated with entities that previously provided transmission service are a rarity. Especially since completion of Fortis, Inc.'s purchase of ITC Holdings, true independence is a fiction.

The history of ITCM's Transco Adder provides an illuminating example of the difficulties of the independence standard even for "true Transcos." In 2007, following the Commission's promulgation of its transmission incentive rules, ITCM sought approval of a 100 basis-point Transco Adder. The Commission found that ITCM met its requirements as a stand-alone Transco and affirmed its policy of preferring the transco structure above others. Even so, the Commission refused to approve the requested adder because ITCM could not prove that its "incentivized" ROE would remain within the zone of reasonableness established several years earlier for the MISO base ROE.[61] The Commission emphasized that its denial of the Transco Adder was without prejudice to ITCM filing another request with a revised discounted cash flow study.[62]

ITCM did not make that filing for many years. During that time, ITCM attracted investment that increased its gross plant in service by more than $1.64 billion – a 235% increase over seven years and grew its rate base by over $1.42 billion (387%). No other transmission owner in the MISO North-Central region came close to matching ITCM's record of percentage rate base increases in that period.

On January 30, 2015, ITCM, confronted by an FPA Section 206 complaint against its base ROE,[63] filed its long-delayed request for a 100-basis point Transco Adder. RPGI and other consumers protested this filing. The Commission ultimately granted ITCM's request, but reduced the adder to 50-basis points, stating that "[U]pon review, we find 100-basis points to be excessive for the Transco Adder at this time. We conclude that 50-basis points is an appropriate size for the Transco Adder, taking into account the interests of consumers and applicants, as well as current market conditions."[64] On rehearing, however, the Commission emphasized that independence from market participants and the ability to raise capital in the future for transmission improvements

[61] *ITC Midwest, LLC,* 121 FERC ¶61,229 at PP39 - 40 (2007).

[62] *Id.* at P 44.

[63] Complaint in *Association of Businesses Advocating Tariff Equity v. MISO*, Docket No. EL14-12, FERC Accession No. 20131112-5303 (filed November 12, 2013). Soon after filing its request for a Transco Adder, a second FPA Section 206 complaint was filed challenging the base ROE for the MISO transmission owners, including ITCM. *See* Complaint in *Arkansas Elec. Coop. Corp. v. ALLETE,* Docket No. EL15-45, FERC Accession No. 20150212-5206 (filed February 12, 2015).

[64] *Midcontinent Indep. Sys. Operator, Inc.*, 150 FERC ¶61,252 at P 45 (2015).

to provide continued benefits - not need, rate effects, or any other factor - determined a Transco's qualification for the Transco Adder.[65]

Little over a month after the Commission's order on rehearing, Fortis, Inc. and ITC Holdings announced their proposed merger.[66] On April 20, 2016, wholesale customers of ITC Holdings' operating companies challenged continuation of the Transco Adder asserting, *inter alia*, that ITC Holdings was no longer completely independent from market participants.[67] The Commission agreed in part, finding that the merger had reduced, but not eliminated the independence of ITC Holdings' affiliates.[68] In reaching this conclusion, the Commission weighed the effect of the merger on the operating companies' integrity of investment planning, capital formation, and investment processing and found that in each area, the companies' independence had been compromised.[69] It therefore reduced the Transco Adder from 50 basis points to 25 basis points, asserting that the reduced level was sufficient to maintain support for the Transco business model.

This experience leads to two conclusions regarding the independence standard, one for "true" Transcos and one for Transcos affiliated with market participants. First, with regard to "true" Transcos, the Commission's application of its independence requirement creates an entitlement to the Transco Adder even when denying the adder may be the most just and reasonable result. In *ITC Midwest*, the Commission increased a base ROE by 50 basis points for a Transco

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[65] *Midcontinent Indep. Sys. Operator, Inc.*, 154 FERC ¶61,004 at PP 29 – 32 (2016). The Commission's orders in this proceeding are the subject of a petition for review before the U.S. Court of Appeals for the D.C. Circuit in *Resale Power Group v. FERC*, Case No. 16-1088 (filed May 19, 2016).

[66] Energy Times, *Fortis to Acquire ITC Holdings for $11.3 Billion* available at https://www.theenergytimes.com/new-utility-business/fortis-acquire-itc-holdings-113-billion (last viewed June 24, 2019).

[67] *Consumers Energy Co.*, 165 FERC ¶61,021 at P 1.

[68] *Id.* at P 68.

[69] *Id.* at PP 69-71.

that was not a new business form with unknown risks. By the time it filed its second request for the Transco Adder, ITCM had nearly a decade-long record of completing over $1.5 billion in transmission system improvements and providing its shareholders with high returns. ITCM did not submit a scintilla of evidence to demonstrate that it would have difficulty attracting future investment and made no new commitments to do anything other than what it was already doing. Creating an entitlement to the Transco Adder at any level under these circumstances is unjust and unreasonable.[70]

To prevent this type of result, if the Commission decides to preserve the Transco Adder, it should limit its availability to the point at which the Transco is formed and files its first FPA Section 205 tariff – a point when the Transco is an unknown entity without a track record of successful project financing, construction, and operation and when an enhanced ROE may be required to obtain financing at a reasonable cost. The Commission should also put time limits on the Transco Adder's effectiveness. At some point (perhaps five to seven years), the Transco ought to be able to function without any base ROE enhancement, just as other, more traditionally structured transmission owners. If the Transco believes it still requires the Transco Adder to attract capital, it should be required to prove that necessity. Ratepayers should not be forced to pay increased rates *ad infinitum* based on nothing more than an entity's business structure rather than its financial need.

Second, with regard to Transcos affiliated with market participants, the Commission should recognize that linking the Transco Adder to independence is a fiction. The project planning, capital formation, and investment processing for affiliated Transcos ultimately cannot help but be

[70] As noted above, RPGI has sought review of the Commission's grant of the Transco Adder by the United States Court of Appeals for the D.C. Circuit.

influenced by other members of its "corporate family." At some level, someone in the corporate structure is making decisions in all three areas that impact both the market participant and the Transco. Someone (hopefully, the Board of Directors) is deciding how to maintain or increase shareholder returns. Even in corporations (like Fortis, Inc.) with decentralized structures,[71] corporate-level decisions about the sources and allocation of funds can influence Transco operations and determine its ability to make transmission improvements.

Consequently, RPGI recommends that the Commission discontinue granting Transco Adders to Transcos affiliated with market participants. If the Commission decides to continue to grant incentives to Transcos, it should make those incentives available only to standalone, truly independent entities (while recognizing that if successful, a "true Transco's" independence is likely to be short-lived).

Question 59: Should a Transco incentive be awarded on a project-by-project basis?

For the reasons stated in RGPI's response to Question 58, Transco Adders should not be awarded on any basis. Awarding the Transco Adder on a project-by-project basis is nothing other than authorizing an incentive-based ROE, which the Commission authorized in Order No. 679 (as clarified in Order No. 679-A) for award for new, non-routine investments in transmission facilities that those projects present special risks or challenges.[72] The Commission should not replace or augment that analysis by automatically awarding a fixed Transco Adder to such projects when they are constructed by Transcos. In addition to unfairly advantaging Transcos at the expense of

[71] Fortis, Inc. 2018 Annual Report at p. 29 (Fortis's "decentralized structure and customer-focused business culture will support the efforts required to meet evolving customers expectations and to work with policy makers and regulators on solutions that are financial sustainable for its utilities." This report is available at https://www.fortisinc.com/docs/default-source/finance-regulatory-reports/annual-reports/fortis-2018-annual-report-final1.pdf?sfvrsn=42767798_2 (last viewed on June 24, 2019).

[72] Order No. 679, 116 FERC ¶61.057 at P 91; *Promoting Transmission Investment through Pricing Reform*, Order No. 679-A, 117 FERC ¶61,345 at PP 51, 60 (2006).

other utilities in the competition for capital, a Transco Adder would virtually ensure that the project's total ROE will be unjust and unreasonable.

The Commission considers a project's risk when determining exactly where in the zone of reasonableness to set the project's incentive ROE. If a Transco's construction of that project adds risk, then the Commission should take that additional risk into account when tailoring the project's incentive ROE to reflect its risk. Awarding an additional Transco Adder would serve only to increase costs for customers while conferring no new benefits on them and result in unjust and unreasonable rates.

Question 60: Should the Transco incentive exclude assets that a Transco buys rather than develops?

If the Commission decides to continue awarding Transco Adders, it should exclude assets that a Transco buys rather than develops. The Commission's purpose in adopting its incentive rules was to encourage the construction of new infrastructure, not "simply increasing rates in a manner that has no correlation to encouraging new investment."[73] By definition, purchasing existing transmission assets does not encourage new transmission investment. Such assets are best addressed through traditional ratemaking techniques, not through incentives intended to encourage rapid addition of truly new transmission facilities.

2. RTO/ISO Participation

Question 61: Should the Commission revise the RTO-participation incentive?

The Commission should discontinue its RTO-participation incentive.[74] The RTO Adder has not proved to be an effective tool for encouraging transmission utilities to join Transmission

[73] Order No. 679, 116 FERC ¶61,057 at P 6.

[74] In these comments, "RTO Adder" has the same meaning as "RTO-participation incentive" and the terms are used interchangeably.

Organizations. But even if the RTO Adder worked when Transmission Organizations were new, unproved entities, it has no place in today's restructured electric industry.

(a) The RTO Adder has not been an effective means for encouraging membership in Transmission Organizations. As noted above, in Order No. 2000, the Commission deemed independent transmission organizations to be essential components of a restructured electric industry."[75] Congress concurred when it enacted Section 219. Section 219(c) requires the Commission to provide for incentives to "each transmitting utility or electric utility that joins a Transmission Organization.[76] In Order No. 679, the Commission chose to implement this mandate by authorizing a "non-generic" ROE adder that would be set on a case-by-case basis. The Commission established only two eligibility criteria for these incentives: (1) a demonstration that a utility has joined a Transmission Organization and (2) an affirmation that this membership is ongoing.[77]

Nineteen years after Order No. 2000's issuance, many of the benefits of Transmission Organization membership that were theoretical in 2003 have been realized, but whether the RTO Adder was even a minor factor in this transformation is open to serious question. Its history in MISO illustrates this point. MISO was formed in September 1998 as an ISO and became the first Commission-approved RTO in 2001.[78] In 2002, the Commission approved an RTO Adder of 50 basis points for the new RTO,[79] but the Commission's determination was vacated on review by the D.C. Circuit because the Commission had not notified parties of its consideration of the adder

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[75] Order No. 2000, 1999 FERC LEXIS 2692 (Part 5) at **7.

[76] NOI, 166 FERC ¶61,208 at P 38.

[77] Order No. 679, 116 FERC ¶61,057 at P 327.

[78] *Midwest Indep. Sys. Operator, Inc.*, 97 FERC ¶61,326 at 62,501 (2001).

[79] *Midwest Indep. Sys. Operator, Inc.*, 100 FERC ¶61,292 at P 31 (2002).

and approved it without considering any record evidence.[80] No utilities withdrew their membership as the result of the court's opinion.

Almost ten years passed before the MISO utilities requested that the Commission authorize a new RTO Adder. During that decade, MISO grew significantly, ultimately expanding from the upper Midwest into the South and becoming one of the largest power grid operators in the world with the responsibility of operating over 65,000 transmission miles of transmission lines connected to more than 196,000 MWs of electric generation capacity.[81] Only when they were confronting a potentially significant base ROE reduction resulting from a pending Section 206 complaint proceeding did the MISO utilities request the RTO Adder's reinstatement.[82]

If the MISO transmission utilities considered the RTO Adder to be an essential, desirable, or even material consideration, they would have filed for it immediately after the D.C. Circuit invalidated the original adder. After all, the court did not find substantive fault with the Commission's order. In its order on remand, the Commission even invited the utilities to make such a filing, observing that "Midwest ISO or the TOs [transmission owners] can make a filing under section 205 of the FPA to include an incentive adder."[83] No filing was forthcoming. It is therefore fair to conclude that at least in MISO, the RTO Adder's only accomplishment has been to further increase transmission rates paid by customers, some of whom (like RPGI members) have been reeling from massive transmission rate increases.

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[80] *Public Serv. Comm'n v. FERC*, 397 F.3d 1004, 1012-1013 (2005).

[81] *See MISO History* at http://timeline.misomatters.org (last viewed on June 24, 2019).

[82] *Midcontinent Indep. Sys. Operator, Inc.*, Docket No. ER15-358-000, Application, FERC Accession No. 20150105-3035 (filed November 5, 2015).

[83] *Midwest Independent Transmission System Operator, Inc.*, 111 FERC ¶61,355 at P 5 (2005).

Consequently, the Commission should not just revise the RTO Adder. It is an incentive that, at least in MISO, has not fulfilled its intended purpose, has no prospect of doing so, and as such, should be discontinued.

(b) ***The continued development of the restructured electric industry has obviated the RTO Adder's underlying rationale for incentivizing continuing Transmission Organization membership.*** Even if the RTO Adder had been even somewhat effective in the early 2000s, the primary rationale for applying it to continuing Transmission Organization members has been supplanted by the Commission's ongoing refinement of its electric transmission policies.

In Order No. 679, the Commission not only authorized RTO Adders for new Transmission Organization members, but also extended the scope of eligibility for the adder to include those utilities that had joined the Transmission Organization before Order No. 679's issuance. According to the Commission, doing otherwise would create "perverse incentives" for the utility to leave one Transmission Organization and move to another where it would qualify for the incentives. The Commission also deemed the exclusion of existing Transmission Organization members from eligibility for the adder to be "unduly discriminatory."[84] In Order No. 679-A, the Commission reinforced this reasoning, characterizing the adder as an inducement for "utilities to join, *and remain in*, Transmission Organizations" to be entirely consistent with Section 219(a)'s requirement of benefitting consumers by ensuring reliability and reducing the cost of delivered power.[85]

In 2018, the U.S. Court of Appeals for the Ninth Circuit held in *California Public Utilities Commission v. FERC* that the Commission had acted arbitrarily and capriciously by granting a

[84] Order No. 679, 116 FERC ¶61,057 at P 331.

[85] Order No. 679-A, 117 FERC ¶61,345 at P 80 (emphasis added).

50-basis point RTO Adder to a utility that had joined an ISO in 1997 – nine years before Order No. 679.[86] The court found, *inter alia*, that the Commission had failed to explain how an incentive designed to encourage a utility to remain in the ISO applied to a utility that, by operation of law, could not withdraw from the ISO. According to the court, the voluntariness of a utility's membership in a Transmission Organization is "logically relevant to the adder," with incentives being justified only for those utilities with the option to withdraw.[87] The court remanded the case to the Commission, which has not yet issued its order on remand.

The Ninth Circuit's opinion points out the Commission's fundamental conceptual error in extending the RTO Adder beyond its original purpose of incentivizing utilities to join Transmission Organizations. Independent Transmission Organizations were essential components of the Commission's restructuring of the wholesale electric industry to provide non-discriminatory, open access transmission for competitive power markets.[88] The Commission first adopted the RTO Adder as an inducement for utilities to join a new type of organization from which they would realize substantial benefits.[89] Joining a Transmission Organization was voluntary, and the incentive was a means for bringing about new industry normal.

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[86] *California Pub. Util. Comm'n v. FERC*, 879 F. 3d 966 (2018).

[87] *Id*., 879 F.3d at 974 - 975.

[88] Order No. 2000, 1999 FERC LEXIS 2692 (Part 5) at **12.

[89] *2003 Pricing Policy Statement*, 102 FERC ¶61,032 at 61,065. In Order No. 2000, the Commission identified the benefits of Transmission Organization membership as:

> [I]ncreased efficiency through regional transmission pricing and the elimination of rate pancaking; improved congestion management; more accurate estimates of [Available Transmission Capacity]; more effective management of parallel path flows; more efficient planning for transmission and generation investments; increased coordination among state regulatory agencies; reduced transaction costs; facilitation of the success of state retail access programs; facilitation of the development of environmentally preferred generation in states with retail access programs; improved grid reliability; and fewer opportunities for discriminatory transmission practices.

Order No. 2000, 1999 FERC LEXIS 2692 (Part 1) at **116 (footnote omitted).

The Commission did not recognize, however, that while continuing membership in MISO was and is voluntary, there exist major *dis*incentives that make the likelihood of withdrawal quite low, at least one of which has been approved since the issuance of Order No. 679. If extending the RTO Adder to incentivize continuing RTO membership ever made sense, it certainly does *not* make sense now.

First, a transmission utility, having joined MISO, can only withdraw its membership from an RTO with applicable federal and state regulatory approvals.[90] Leave to withdraw is not a given. To obtain Commission approval, a utility must satisfy the three-part test first articulated *Louisville Gas & Electric Co*. [91] and the Commission may establish such conditions as it deems necessary to assure that the withdrawal's result is just, reasonable, and nondiscriminatory.[92]

Moreover, in MISO, the withdrawing utility must comply with the "hold harmless" provision of the MISO TO Agreement that requires the utility to continue to serve customers with contracts executed before the notice of withdrawal at the same rates, terms, and conditions that would have been applicable if there were no withdrawal until the contract's expiration.[93]

[90] Agreement of Transmission Facility Owners to Organize the Midcontinent Independent System Operator, Inc., a Delaware Non-Stock Corporation ("MISO TO Agreement"), Article Five, Section III, available at https://cdn.misoenergy.org/Rate%20Schedule%2001%20-%20Transmission%20Owners%20Agreement47071.pdf (last viewed on June 24, 2019).

[91] *Louisville Gas & Electric Co.*, 114 FERC ¶61,282 at P 27 (2009). In this case, the Commission referred to four criteria for withdrawal, but held that the first requirement (the effect of withdrawal on the RTO and its remaining members) was fully satisfied by the "hold harmless" of the MISO TO Agreement discussed *infra*. Later cases refer to the three remaining requirements for withdrawal as those that must be satisfied for withdrawal: (1) the withdrawal must satisfy the terms of the applicant's contractual obligations as they relate to RTO withdrawal; (2) the proposed replacement arrangements must comply with the Commission's *pro forma* OATT and/or the standard of review applicable to proposed tariff provisions that differ from the *pro forma* OATT; and (3) the replacement arrangements must be just, reasonable, and not unduly discriminatory. *PJM Interconnection, LLC*, 135 FERC ¶61,198 at P 5 (2011).

[92] *See PJM Interconnection, LLC*, 135 FERC ¶61,198 (2011) and *Midwest Indep. Transmission Sys. Operator, Inc.*, 135 FERC ¶ 61,204 (2011) (Accepting American Transmission Systems, Inc.'s withdrawal from MISO and realignment to PJM and establishing conditions for the change).

[93] MISO TO Agreement, Article Five, Section IIA.

In addition, under Schedule 39 of the MISO Open Access Transmission Tariff, a withdrawing transmission utility must bear a continuing financial responsibility for its share of network expansion projects (known as Multi-Value Projects) approved prior to the effective date of the withdrawal.[94] A withdrawing member's share of the projects' costs could be considerable.[95]

But perhaps as a practical matter, the greatest disincentive to withdrawal is the high degree of integration of the MISO transmission owners' systems from both operating and planning perspectives. MISO has matured as an organization since the issuance of Order No. 679 and its transmission owning members and their ratepayers have made such a major commitment of resources to MISO participation that withdrawal is nearly unthinkable. In short, events and the passage of years have taken away the purpose of an incentive for continuing Transmission Organization membership.

And this is as it should be. An incentive should not have a life of its own. It is a tool used to achieve a specific objective. Once that objective has been reached, the tool has fulfilled its purpose and must be set aside. Consequently, the Commission must either discontinue the RTO Adder entirely or limit its scope to new Transmission Organization members only.

Question 62: Should the Commission consider providing incentives other than ROE adders for utilities that join RTO/ISOs, such as the automatic provision of CWIP in rate base or the abandoned plant incentive for all transmission-owning members of an RTO/ISO? If so, what other types of incentives would be appropriate?

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[94] MISO Open Access Tariff Schedule 39 (available at https://www.misoenergy.org/legal/tariff/ (last viewed on June 24, 2019). *See also MISO Transmission Owners v. FERC*, 860 F.3d 837 (2017).

[95] To provide an order of magnitude, MTEP 2018 proposed, and the MISO Board of Directors approved, a $3.3 billion, 442-project transmission system expansion plan. Press release available at https://www.misoenergy.org/about/media-center/miso-approves-2018-transmission-plan/ (last viewed on June 24, 2019).

FPA Section 219(c) requires the Commission to provide incentives to each utility that joins a Transmission Organization. As RPGI noted in its response to Question 61, expanding this mandate to authorize incentives for *all* transmission-owning members (including continuing members) of such organization is unnecessary, inadvisable, and likely to result in excessive, unjust, and unreasonable rates. If there are specific projects for which the incentive would be appropriate, the Commission has developed standards and procedures for considering the projects' eligibility and tailoring incentives to meet the projects' particular requirements and risk profile.

With regard to new members, RPGI strongly believes that given the success of Transmission Organizations such as MISO over the past fifteen years, the manifest benefits of membership should be a more than sufficient incentive for joining. In effect, the Commission, by nurturing Transmission Organizations, has fulfilled Section 219(c)'s objective. Successful organizations attract members. The success of Transmission Organizations has become the most powerful recruiter of new members and the most effective membership incentive. There is no need for additional incentives.

Question 63: If the Commission continues to provide ROE adders for RTO/ISO participation, what is an appropriate level for an ROE adder?

For the reasons noted in RPGI's response to Question 61, the Commission should not provide ROE adders for continuing participation in a Transmission Organization. At most, the RTO Adder should be granted only to transmission utilities joining a Transmission Organization and only for a fixed period of time after joining, as noted below.

Question 64: Should the RTO-participation incentive be awarded for a fixed period of time after a transmission owner joins an RTO or ISO?

For the reasons noted in RPGI's response to Question 61, the Commission should not authorize RTO Adders for continuing participation in a Transmission Organization. If the

Commission determines that an RTO Adder is required, it should limit the adder to a period of no more than five years. By limiting the RTO Adder's effectiveness to a set period, the amount of the adder could be calculated as a lump sum at the time the utility becomes a Transmission Organization member and recovered over a period determined by the Commission to be in the best interests of both the utility and its customers. The Commission proposed a version of this approach in the *2003 Pricing Statement*.[96] If a new membership incentive is required, this approach would be far more equitable than an open-ended adder that has no expiration and is applied to a rapidly growing rate base.

Question 65: Should the RTO-participation adder be awarded on a project-specific basis?

RTO Adders should not be awarded on a project-by-project basis. Awarding an RTO Adder on a project-by-project basis is nothing other than authorizing an incentive-based ROE, which the Commission approved in Order No. 679 (and clarified in Order No. 679-A) for award when justified, for new, non-routine investments in transmission facilities that present special risks or challenges.[97] The Commission should not replace or augment that analysis. Awarding an RTO Adder in such circumstances would increase, if not assure, the likelihood that the project's total ROE will be unjust and unreasonable and would serve only to increase costs for customers while conferring no new benefits on them.

Question 66: In Order No. 679, the Commission found that "the basis for the incentive is a recognition that benefits flow from membership in such organizations and the fact that continuing membership is generally voluntary." Should voluntary participation remain a requirement for receiving RTO/ISO incentives?

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[96] *2003 Pricing Policy Statement*, 102 FERC ¶61,032 at P 25.

[97] Order No. 679, 116 FERC ¶61,057 at P 91; Order No. 679-A, 117 FERC ¶61,345 at PP 51, 60.

For the reasons noted in RPGI's response to Question 61, the Commission should not provide RTO Adders or other RTO/ISO incentives for continuing participation in a Transmission Organization. Although RPGI believes that incentives for new members in Transmission Organizations are not required at this time (*see* RPGI response to Question 62), if the Commission wishes to continue to encourage utilities to join Transmission Organizations, it should define a package of incentives that would be available until a date certain by which it expects all transmission companies to be Transmission Organization members. Past that date, the incentives would expire.

Respectfully submitted,

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June 26, 2019

ATTACHMENT A

ATTACHMENT A

RPGI MEMBERS

Amana Society Service Co.
Anita Municipal Utilities
City of Afton
City of Buffalo
City of Danville
City of Guttenberg (as of 01/01/2019)
City of Pocahontas
City of West Liberty
Coggon Municipal Utilities
Dysart Municipal Utilities
Farmers Electric Cooperative–Kalona
Grand Junction Municipal Utilities
Hopkinton Municipal Utilities
La Porte City Utilities
Long Grove Municipal Electric Utilities
Mt. Pleasant Municipal Utilities
New London Municipal Utilities
Odgen Municipal Utilities
Sibley Municipal Utilities
State Center Municipal Utilities
Story City Municipal Electric Utility
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