

Competitive Transmission Is Good And It Is Here To Stay

Law360, New York (April 16, 2015, 12:38 PM ET) --

Competitive transmission is a key new frontier as the nation confronts its long-term need for new energy infrastructure. Created by the Federal Energy Regulatory Commission through Order No. 1000, policymakers at FERC had the vision to ask: “Why can’t we do with transmission what we did with generation?” Can competition work with the ownership and operation of transmission? Indeed, competition, while sometimes complicated, is meant to bring out creative, market-driven solutions that achieve significant cost savings. Can competition work with the ownership and operation of transmission? It’s been almost four years now since Order No. 1000 was issued and the real-time implementation of competitive transmission is unfolding before our eyes. So how is it meeting these objectives?



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Is Competitive Transmission Working?

So far, yes. Regional transmission organizations and independent system operators are off and running with competitive transmission solicitations. PJM Interconnection LLC and the California Independent System Operator are leading the way, so far. Both PJM and the California ISO are making the most progress on competitive solicitations, while other RTO and ISO programs are in various stages of implementation. For example, the Midcontinent Independent System Operator recently wrapped up its pre-qualification process for would-be bidders, but has indicated that it does not expect to introduce new projects until 2016.

In both the California ISO and PJM, these solicitation processes are yielding highly energized competition, creative ideas and cost efficiencies. There has been no shortage of well-qualified competitors and no shortage of ideas. This strong supply-side response is already driving down costs for consumers. Cost containment ideas that were not part of the landscape before competition are now at the forefront of implementation discussions nationwide. FERC, for its part, continues to stand behind Order No. 1000, as evidenced by its series of RTO and ISO compliance orders upholding the pillars of Order No. 1000.

Which Model Works Best?

Perhaps it is no surprise that PJM and California ISO have taken different approaches to competitive

transmission. PJM identifies the problem and asks bidders to propose solutions. For example, PJM indicates that a set of transmission elements are overloaded and asks bidders to identify upgrades to resolve the problem. The California ISO, on the other hand, provides the solution, and asks bidders to propose the best and most cost-effective means to achieve that solution. For example, the California ISO may state that a transmission line of a certain capacity needs to be constructed between two existing substations and then invite parties to identify how they would construct the transmission line between these two points. This difference of approach is reflective of the historic planning practices of the two organizations.

PJM, for example, historically identified overloads on the transmission system and looked to the transmission owners to propose upgrades to resolve the overloads. The California ISO's approach to competitive transmission creates more defined, but more constrained competition. Because the basic upgrade is already defined, the competition focuses on practical aspects of implementation, such as land rights, operation and cost. That makes the competition easier to implement and yields strong practical results, although perhaps at the expense of leaving some creative ideas on the cutting-room floor. Notably, however, the California ISO recently chose its first "nonincumbent" transmission winner, illustrating that the process is working.

In comparison, PJM's approach allows for more creativity — witness the dozens of proposals for Artificial Island — but at the cost of complexity in the decision-making process. While PJM's process certainly puts more burden on the decision makers at PJM, the benefit is that it captures both the creative ideas and efficient implementation of bidders, which ultimately will be to the ratepayers' benefit. If PJM can figure out how to harness its process and make it work, it will reflect a more pure vision of competitive transmission that may yield different, greater and fuller fruit.

What About Artificial Island?

Artificial Island is the reef that PJM currently is facing. Rather than talking about competitive transmission, PJM put its process to the test with an aggressive laboratory effort in Artificial Island. This is an area in Southern New Jersey where the Salem and Hope Creek nuclear generators are located, which has been historically constrained. As PJM said from the beginning, Artificial Island is intended to prove out its processes for competitive transmission, rather than represent its full Order No. 1000 implementation. But Artificial Island already has been a success. It has yielded dozens of proposals, with creative ideas for new transmission facilities across a broad spectrum. It has brought out vigorous competition among many new market entrants, which has now been reduced to a "final four." While it has been contentious at times, there is no real substitute for actually going through the process. The learning that comes out of Artificial Island will forge the process for competitive solicitations in PJM. Change isn't always easy.

Haven't I Seen You Somewhere Before?

Competitive transmission follows on the heels of competitive generation. Under the Public Utility Regulatory Policies Act of 1978, through the exempt wholesale generator era and beyond, competitive generation started small under PURPA with independent power producers developing small renewable generating facilities and cogeneration, which was not at the core of the vertically integrated utility baseload model. Competitive transmission, however, is starting off differently. Competitive transmission involves competition for the largest and most significant projects. This means new entrants must bring their "A game" from the beginning. It can be a steep learning curve.

Unlike competitive generation, however, this isn't a competition to provide service. The RTOs and ISOs provide transmission service. Rather, it is a competition to design, construct and own the transmission facilities over which the RTOs and ISOs will then provide transmission service in a regulated environment. In fact, by creating the RTOs and ISOs, the transmission owners planted the seeds for competitive transmission to take root.

Cost Containment Is the New Frontier

As mentioned above, one of the key implementation issues is how to balance the need for competition with cost containment. Cost containment and new transmission have not always been thought of together. While initially given more talk than action, cost containment is quickly becoming a critical determinant for competition between highly qualified entrants. New cost containment ideas, including cost caps, are being created and included in submittals at a breathtaking pace. This is among the most important components in a successful competitive transmission bid today. And this is proving to be true both with the California ISO and PJM. It's not clear that the RTO and ISO decision-making processes have fully caught up with cost containment proposals, but it is clear that it is a key factor RTOs, ISOs, FERC and ratepayers have been looking for. The speed with which cost containment has become a critical factor is astounding.

It remains to be seen exactly how the RTOs and ISOs will integrate the cost containment criteria into their decision-making. It is also unclear how RTOs, ISOs and potentially FERC will enforce cost containment commitments, given the potential for bidders to face cost overruns down the road. These same issues, of course, have been addressed in competitive generation and can be addressed here as well. Stay tuned.

Is There Still a Role for Merchant Transmission?

In our view, the answer is yes. Merchant transmission, as defined here, means competitive transmission projects developed outside of the Order No. 1000 competitive solicitation process. The answer is yes, because the Order No. 1000 competitive solicitation processes are focused on transmission upgrades within the RTOs and ISOs. For example, currently there is no RTO or ISO process for the solicitation of projects between RTOs and ISOs. These projects, which require a combination of creativity, vision and patience, continue to be needed, and will continue to evolve outside of the current competitive solicitation process, although that too could change if FERC continues to find success in implementing Order No. 1000.

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