Cost Containment for Competitive Transmission
Preliminary Thoughts on Design

New England States Committee on Electricity

May 16, 2019

This presentation is for discussion. Any views expressed in this presentation should not be construed as representing those of NESCOE, any NESCOE manager, or any individual state.

Transmission Costs

- ISO-NE has noted the diverse benefits of transmission investments, including enhanced system reliability and lower priced power.
- These benefits come at a cost.
  - For most residential retail electric customers in N.E., transmission costs account for between 11% to 18% of total retail rates.
  - Transmission charges have risen dramatically over the last decade, increasing almost every year from 2008 and, over that decade, growing from roughly $869 million in 2008 to $2.25 billion in 2018.
  - As of the last RSP, another $4 billion in additional transmission investments was planned

Source: 2018 CLG Report; 2017 RSP

Containing Transmission Costs in the 2019 RFP

- As a region, we should seek to achieve the benefits of transmission at the lowest cost to consumers making those investments.
- The competitive process under Order 1000 has the potential to encourage cost containment in the development of transmission infrastructure.
- ISO-NE has indicated that it will issue an RFP for Boston reliability needs at the end of 2019
  - Given that the RFP will be New England's first experience with a competitive transmission process and that it will be issued in relative short order, it is imperative that we start thinking through the most effective cost containment approaches now.

Other Regions

- LS Power Presentation at January 23, 2019 TC meeting provided examples of others regions (CAISO, SPP, MISO) where FERC-approved tariffs include cost containment provisions as part of evaluation/selection criteria for competitive transmission projects under Order 1000.

- LS Power also presented on active efforts in PJM to develop procedures on cost caps and cost containment as part of its Order 1000 competitive transmission process.
  - Noted process underway in NYISO as well.

State Models (examples)

- Three State Joint Clean Energy RFP (2015)
  - Expressed strong preference for cost containment while not foreclosing cost-of-service bids: "proposals including cost containment features such as fixed price components, cost overrun restrictions, or other cost bandwidth provisions to limit customer risk will be viewed more favorably."
  - Projects without "significant cost containment features" are unlikely to be selected and "strongly encourages" bidders to include these elements in their proposals.
- MA 83D RFP (2017): "Cost of service is allowed for transmission pricing proposals, however all proposals must include significant cost containment features (examples of such features include, fixed price components, cost overrun restrictions, or other cost bandwidth provisions) Bids that limit customer risk to a greater degree will be viewed more favorably."

How to reform?

Goal: Revise the evaluation and selection criteria to give weight to projects that include binding cost containment features.

But

Cost containment is complex and implementation details require careful deliberation. Regional collaboration is important in designing appropriate and effective mechanisms.

Construction Cost or Revenue Requirements?

- Consumers are most interested in the costs they see on their monthly bill - not necessarily in construction costs
- Maybe we should be comparing annual revenue requirements of projects over comparable lengths of time - not project costs?
- Many items go into calculating revenue requirements in addition to construction costs.
- Developers could be asked to submit the expected annual revenue requirements over a comparable length of time (20 years, for example? Longer?) as part of their project submittal
- The NPV of total revenue revenue requirements could be one element of comparison

Elements of Revenue Requirements

- Construction Cost
- ROE
- Capital Structure
- O&M
- Property Tax
- A&G
- Other

Examples of Cost Containment Mechanisms

- Construction Cost Cap
  - Firm
  - Adjustments allowed out of set boundaries?
  - Adjustments allowed for certain items?
- ROE
  - Agree to lower than otherwise allowed?
  - Fixed for some period, then 205 permitted?
- O&M fixed for some period or straight passthrough?
- Risk Sharing?
- Cap on Annual Revenue Requirement
  - For a fixed time or for length of project?

Type of Risks that Developer could agree to absorb

- Approvals, Permitting, and Routing
- Land acquisitions and rights
- Subsurface issues
- Environmental assessments and risks
- Design and engineering
- Equipment and supplies procurement
- Total project construction cost risk
- Inflation risk

How to compare projects?

- So many variables make comparisons challenging
- Just looking at construction costs ignores many possible ways that projects - and project costs - can differ
- One suggestion – require all developers to submit 20-year revenue requirement estimate for their project to allow comparisons
- Evaluate the NPV for all projects using a common discount rate
- Evaluate the amount of risk for consumers from each project
  - Could involve rigorous risk analysis
    - Might be too complex and time consuming; or
  - Rank on qualitative factors, high medium and low
    - Easier but not as accurate

Conclusion

- Cost Containment provisions are critical and should be addressed in all bids
- Method of comparison and containment may vary by bid making comparison complex and difficult
- We appreciate the opportunity to express strong interest in beginning this conversation now and welcome others' views here and at subsequent meetings to help inform our own.