Comments on NYISO's Proposed Treatment of Capital Costs in Proposed Public Policy Transmission Projects

The Transmission Owners ("TOs")[1] respectfully submit these comments on the New York Independent System Operator, Inc.'s ("NYISO") proposal, "Cost Containment Metric for Transmission Project Evaluation in Public Policy Process."[2] While the TOs believe that cost containment is appropriately within the jurisdiction of the Federal Energy Regulatory Commission ("FERC") and best left to the FERC rate settlement process, in the interest of compromise, the TOs are agreeable to considering certain cost containment principles within the NYISO Public Policy Transmission Project solicitation process. The TOs acknowledge and appreciate the work NYISO has done to date in modifying its proposal in response to stakeholder comments, and offers these comments to help further refine the proposal.

Form of Cost Containment

As noted in previous meetings, the TOs' primary concern with NYISO's original proposal[3] was its requirement that transmission developers that elect to include cost containment in their bids would have to agree to a "hard" cost cap, i.e., such that no recovery of incurred expenses above the cap (even if prudently incurred) may be obtained. The TOs, therefore, support NYISO's modification of its proposal to include the consideration of a "soft" cost cap, where the costs of incurred expenses above the cap are shared between investors and customers.

However, NYISO's current proposed consideration of "soft" cost caps appears to be limited to rate designs where the developer agrees to forego recovery of a percentage of incurred expenses above the cap. There are alternate rate designs that have been demonstrated to achieve similar cost sharing outcomes, without requiring a developer to waive its right to recover prudently incurred costs. For example, the recent transmission rate settlements for public policy transmission projects proposed by New York Transco, LLC ("NY Transco")[4] and NextEra Energy Transmission New York, Inc. ("NEETNY")[5] achieve 80/20 cost overrun sharing (where customers bear 80% of the costs of cost overruns and investors bear the remaining 20%) through adjustments to return on equity ("ROE") that achieve a comparable benefit to customers, and balances that with the needs of the developer to construct the project in a timely manner. This rate design effectively balances ratepayers' interest in incentivizing cost discipline with a developer's need for certainty.

NYISO's current proposal cautions that it is "not clear how NYISO would apply reduced ROE/incentives in [the] absence of [a] FERC order accepting/approving these items in advance of project solicitation." Contrary to NYISO's statement, there are already two existing FERC settlements which lay out how such a cost sharing approach works. The NY Transco settlement further provides that the rate design may also be applied to future projects selected by the NYISO. This rate design is a reality today, as it has already

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[1] For the purposes of these comments, the Transmission Owners include Central Hudson Gas & Electric Corporation; Consolidated Edison Company of New York, Inc.; Niagara Mohawk Power Corporation d/b/a National Grid; New York State Electric & Gas Corporation; Orange & Rockland Utilities, Inc.; and Rochester Gas & Electric Corporation.

[2] Available at https://www.nyiso.com/documents/20142/6786453/Cost_Containment_Eval%20Proposal%2020190522.pdf/fb0a93ad-a590-151a-c7eb-57601159ac87

[3] Available at https://www.nyiso.com/documents/20142/3740322/Cost%20Containment%20NYISO%20Straw%20Proposal.pdf/41ef0ab0-adce-f5db-8114-6afd539ac10e

[4] FERC Docket ER15-572

[5] FERC Docket ER16-2719

been proposed and approved in New York. Second, it is ultimately FERC that has jurisdiction over transmission rates and on the overall rate design that will implement the soft cap. As such, NYISO's cost containment process must provide flexibility for developers to make an appropriate proposal to the NYISO while working with the FERC and other parties, in the rate application process, to implement the proposed cost cap. The TOs are committed to working with NYISO to develop an effective process to balance consumer and transmission developer/owner interests.

Quantitative Consideration of Cost Containment Proposals

NYISO proposes both a quantitative and qualitative metric for assessing cost-contained bids. For the quantitative metric, NYISO would use the developer-proposed cap for contained capital cost elements, and the independent cost estimate for cost elements excluded from cost containment. For developers agreeing to a "hard" cap, NYISO will use the developer's estimate without adjustment; for "soft" caps, NYISO will adjust the capital cost based on the proposed cost-sharing percentage. Such an approach must be able to fairly support the analysis of developer's proposal. Doing so raises some concerns. The TOs disagree with the tentative approach laid out in NYSO's presentation, where the NYISO would use the (lower) independent cost estimate rather than the developer proposal. In all cases, the NYISO should use the developer's cost estimate. This is because the developer agrees in its bid to be contained by its own cost estimate, <u>not</u> the independent cost estimate.

However, relying on the developer's cost estimate does raise concerns when that estimate is materially higher or lower than the independent cost estimate. If the developer's cost estimate is higher, it could render the cost containment mechanism relatively meaningless. If it is materially lower, and the project comes in significantly above the cost cap, it could result in disputes over exclusions and abandoned projects. To address these concerns, a risk analysis approach would be more useful than the NYISO's proposal to adjust developer bids based on whether the developer proposes a hard or soft cost cap. Rather, NYISO should use the developer's cost estimate for <u>all</u> projects¸ and evaluate the customer exposure and project risk through a separate risk factor metric.

Qualitative Consideration of Cost Containment Proposals

NYISO's proposal for a new qualitative metric addresses the issues identified above. This metric would consider the form of cost containment and its ability to protect customers from capital cost overruns. However, the TOs are concerned that this metric as proposed by NYISO is not well-defined. Moreover, it is not clear how it would be applied to project proposals.

There must be a clear framework for the application of a separate cost containment metric. NYISO should publish ahead of each solicitation a framework for how the risk factor would be calculated. For example, NYISO could calculate a risk factor based on two factors:

1. The type of cap proposed by the developer (hard vs soft vs no cap and level of cost-sharing), which would address the potential exposure to ratepayers; and

2. The difference between the independent cost estimate and developer bid, which would address the amount of risk the Developer is assuming and the credibility of the bid.

NYISO could develop a matrix considering these two factors and calculate a combined risk factor that would feed into its analysis, and would then be provided to stakeholders as a metric in the NYISO selection process. As shown in the table below, NYISO could assign different levels of risk to each of the two factors, and multiply them together to calculate a single risk factor that would be used as a metric in the analysis. The TOs believe this approach is preferable because it would provide clear guidance to developers on exactly how their cost containment proposals will be considered, and a transparent process for NYISO to follow in calculating the risk factor.

SECO Estimate vs. Developer Bid	Risk Factors	Type of Cost Cap										
		Hard Cap	10/90	20/80	30/70	40/60	50/50	60/40	70/30	80/20	90/10	No cap
		0.15	0.3	0.35	0.4	0.45	0.5	0.55	0.6	0.65	0.7	0.9
>50%	0.90	14	27	32	36	41	45	50	54	59	63	81
>30%	0.30	5	9	11	12	14	15	17	18	20	21	27
>10%	0.20	3	6	7	8	9	10	11	12	13	14	18
+/- 10%	0.10	2	3	4	4	5	5	6	6	7	7	9
<10%	0.15	2	5	5	6	7	8	8	9	10	11	14
<30%	0.25	4	8	9	10	11	13	14	15	16	18	23
<50%	0.80	12	24	28	32	36	40	44	48	52	56	72

Other Proposal Elements

The TOs agree with NYISO's proposal to limit the scope of cost containment to capital costs. The TOs also agree with NYISO that cost containment implementation and rate issues not addressed in NYISO's cost containment proposal should be determined in the FERC ratemaking process.

In addition, The TOs understand that NYISO's proposal relates only to the Public Policy planning process. The reliability and economic planning processes may warrant different treatment, due to their very different goals (*i.e.,* to maintain the reliability of the bulk power system and address transmission system congestion, respectively). NYISO appropriately notes in its proposal, as it has stated in stakeholder meetings, that further discussions will be required as part of its Comprehensive System Planning Process project to evaluate whether and how to apply cost containment to those processes.

Finally, the TOs generally agree with the cost elements listed by NYISO as "Proposed Included Elements" and "Proposed Excluded Elements"/"Proposed Excusing Conditions." Specifically the TOs agree that exclusions from cost containment should include project omissions or delays due to the actions or omissions of a third party, *Force Majeure* events, changes in laws or regulations, system upgrades determined by the NYISO in one of its interconnection processes, material modifications to scope or routing, actions or inactions of regulatory or governmental entities, and O&M costs. However, the category of "Cost Containment Exclusions" should also include environmental mitigation/remediation, other unknown site conditions, and increases in commodity prices, currency risk, and interest rates.

Conclusion

The NYISO's stated intent is to have a cost containment proposal in place prior to the next public policy solicitation. While NYISO has made headway in expanding the scope of its proposal to consider "soft" cost caps, additional refinement is needed to allow the proposal to be workable for future solicitations, and to be clear what is left for FERC to implement as part of its ratemaking authority. The TOs thus urge the NYISO to continue to work with stakeholders to address stakeholder concerns before advancing the proposal to a vote. We look forward to working with the NYISO and stakeholders as the proposal moves forward.