

Cost Containment Mechanism for Public Policy Transmission Planning Process

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Business Issues Committee

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Objective

- The NYISO proposes to amend the Public Policy Transmission Planning Process in the OATT to establish the treatment of cost containment in the project proposal, evaluation and selection, Development Agreement, and cost recovery processes.
- Assuming a positive stakeholder vote and Board approval, the NYISO plans to make a Section 205 filing so that the cost containment provisions will be accepted or approved by FERC in its tariff. Developers would be able to use those procedures in proposing projects as solutions to any Public Policy Transmission Needs that are identified by the New York State Public Service Commission.

Cost Containment Proposal Overview

- A Developer that proposes a solution may voluntarily provide a capped amount for defined categories of capital costs, and may only rely on the permitted excusing conditions to recover costs over those amounts.
- The NYISO will memorialize the capital cost capped amount and the excusing conditions in the Development Agreement it enters into with the Developer.
- The Development Agreement and Rate Schedule 10 will require the Developer to include the capital cost capped amount and excusing conditions in its revenue requirement filing with the Commission to obtain cost recovery under Rate Schedule 10.

Cost Containment proposal Overview (cont.)

- Cost containment considered in Public Policy Process will be limited to capital costs only
- Evaluation methodology must be feasible for NYISO implementation
- Consistency across projects must be maintained
- Consideration of cost containment must not add to evaluation time and lengthen Public Policy Process
- Rate and rate recovery issues other than those set forth for cost containment in Section 31.4 and Rate Schedule 10 will be addressed by FERC.
- Treatment of cost containment for upgrades to existing Transmission Owner transmission facilities by another developer will be addressed when rights to build and own such upgrades is addressed in the tariff.

Capital Cost Categories

- **Total project capital cost used in evaluation and selection: Included + Excluded Capital Costs**
- **Included Capital Costs: Developer may voluntarily propose cost containment for defined categories of capital costs**
- **Excluded Capital Costs: NYISO and the independent consultant will estimate the excluded capital costs, such as interconnection costs**
- **Developers may propose either a hard cap or a soft cap, as defined below:**
 - **Hard cap:** A hard cap for capital costs is defined as an amount (the cap) over which the Developer agrees not to recover capital costs from ratepayers
 - **Soft cap:** A soft cap for capital costs is defined as an amount (the cap) above which excess capital costs are shared between shareholders and ratepayers based on a defined percentage; Developers would define the percentage of risk sharing as part of their cost containment proposal. Developers percentage of cost sharing under the soft cap shall be at least 20 percent.

Cost Containment: Included Elements

- Capital costs include the cost of contract work, labor, materials and supplies, transportation, special machine services, shop services, protection, injuries and damages, privileges and permits, engineering services, reasonably expected environmental site remediation and environmental mitigation costs as defined in the tariff, general administration services, legal services, real estate and land rights, rents, studies, training, asset retirement, and taxes
- Developers may opt to include or exclude costs of real estate/rights of way they do not own

Cost Containment: Excluded Elements

- i.** system upgrades determined by the ISO in one of its interconnection processes;
- ii.** debt costs, allowance for funds used during construction (“AFUDC”), and other representations of the cost of financing the transmission project during the construction timeframe that may be included as part of the capital cost of the project when it enters into service or as otherwise determined by FERC;
- iii.** unforeseeable environmental remediation and environmental mitigation costs including a change in the extent of contamination, as defined in the tariffs;
- iv.** real estate costs for existing rights-of-way that are part of the proposed Public Policy Transmission Project, but are not owned by the Developer, that Developer chooses not to include as Included Capital Costs pursuant to Section 31.4.5.1.8.1.

Cost Containment: Proposed Excusing Conditions

The Developer is excused from the Cost Cap on recovering the Included Capital Costs of its Public Policy Transmission Project only to the extent the costs arise from one of the following excusing conditions:

- A. Transmission Project changes, or delays, or additional costs that are due to the actions or omissions of the ISO, Connecting Transmission Owner(s), Interconnecting Transmission Owner(s), or Affected Transmission Owner(s);
- B. A *Force Majeure* event as defined in the Development Agreement and subject to the *Force Majeure* requirements in Section 15.5 of the Development Agreement;
- C. Changes in laws or regulations, including but not limited to applicable taxes;
- D. Material modifications to scope or routing arising from siting processes under Public Service Law Article VII or applicable local laws as determined by the New York State Public Service Commission or local governments respectively; and
- E. Actions or inactions of regulatory or governmental entities, and court orders.

Cost Containment—Evaluation Overview

The NYISO will consider cost containment proposals in both a quantitative and qualitative manner:

- **Use in Quantitative Cost Metrics:** Depending on several factors, the NYISO will use the proposed cap for contained capital cost elements (Included Capital Costs) to estimate the total capital cost of the project that is used in existing quantitative cost metrics.
- **Qualitative Evaluation:** In addition, the NYISO will assess any proposed cap qualitatively through a new metric. The additional metric is intended to factor in cost containment as one metric among a host of metrics the NYISO may consider to evaluate, assess and select the more efficient or cost effective transmission project to meet a Public Policy Transmission Need.

Quantitative Factors – Hard Cap

- A hard cap for capital costs is defined as an amount (the cap) over which the Developer agrees not to recover costs from ratepayers for contained capital costs
- The NYISO will use the Developer's cost cap as the estimate for Included Capital Costs plus its independent consultant's estimate of the Developer's Excluded Capital Costs to calculate a total project capital costs, whether the Developer's cost cap is above or below the independent consultant's cost estimate
- The NYISO will use the total capital cost to assess the performance of transmission projects under the cost-based selection metrics, including capital cost and cost per MW

Quantitative Factors – Soft Cap

- **Soft cap:** A soft cap for capital costs is defined as an amount (the cap) above which excess costs are shared between shareholders and ratepayers based on a defined percentage
- If the Developer's soft Cost Cap for the Included Capital Costs is above the amount estimated by the NYISO's independent consultant, the NYISO will rely on the Developer's amount for the Included Capital Costs to calculate the total capital cost of the Developer's Public Policy Transmission Project.
- If the Developer's cost cap is below the independent consultant cost estimate, the NYISO will calculate an **adjusted estimate for contained capital costs for use in the quantitative cost metrics**
 - The adjusted estimate will be based upon the amount of financial risk that the Developer proposes to assume
 - The adjusted estimate for contained capital costs will be calculated by multiplying the difference between the Developer's capital cost cap and the independent consultant estimate (for the same facilities) by the risk percentage assumed by ratepayers
 - The NYISO will add the ratepayer risk exposure amount to the Developer's cost cap, plus excluded capital costs, and use the total for its quantitative metrics

Example of Percentage Cost Sharing

	80/20 Risk Share		50/50 Risk Share		0/100 Risk Share	
	Contained Costs	Excluded Costs	Contained Costs	Excluded Costs	Contained Costs	Excluded Costs
Developer Proposal	100	75	100	75	100	75
Independent Estimate	200	75	200	75	200	75
Adjusted Estimate	180	75	150	75	100	75
Total Capital Costs for Evaluation	255		225		175	

Qualitative Metric

- **A new, separate metric will consider cost containment proposals on a qualitative basis. This new metric will consider:**
 - The effectiveness of the proposed Cost Cap in providing an incentive to the Developers to contain their Included Capital Costs, *i.e.*, how aligned is the Developer's incentive to maximize its profits by avoiding cost overruns compared to the level of risk exposure to consumers, and what degree of risk is the Developer assuming to pay for cost overruns
 - The effectiveness of the proposed Cost Cap in protecting ratepayers from Included Capital Cost overruns
 - The magnitude of the difference between the Cost Cap and the independent cost estimate

Cost Containment Commitment in Development Agreement

- *Pro Forma* Development Agreement amended to include selected Developer's Cost Cap and commitment to file and abide by Cost Caps
- Failure to file or seeking cost recovery in excess of Cost Cap is considered breach of the agreement
- Agreement contains *Mobile Sierra* clause to preserve treatment of cost containment under public interest standard

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Developer's Responsibility to File Cost Cap at FERC via Rate Schedule 10

The selected Developer must file with FERC as part of its required rate filing for cost recovery under Rate Schedule 10 (OATT Section 6.10), any Cost Cap that it proposed for its Public Policy Transmission Project, including the excusing conditions.

- If the Developer proposed a hard Cost Cap, the Developer must file as such.
- If the Developer proposed a soft Cost Cap, the Developer must achieve the percentage cost sharing that it submits to the NYISO in its proposal either:
 - I. through foregoing rate recovery of that percentage of capital costs in excess of the soft Cost Cap or
 - II. through an alternative rate mechanism that may adjust rate recovery through only a reduction in the return on equity and any applicable incentives solely on the amount in excess of the soft Cost Cap.

The alternative rate mechanism must achieve a rate recovery reduction for the percentage of Included Capital Costs in excess of the soft Cost Cap that is equal to or better for ratepayers in the total long run revenue requirement on a present value basis

Tariff Amendments for Approval

- **Four tariff sections posted for approval by the BIC:**
 - OATT Section 31.1 – Definitions
 - OATT Section 31.4 – Public Policy Process
 - OATT Section 31.7 – Development Agreement
 - OATT Section 6.10 – Rate Schedule 10
- **Reviewed and revised at ESPWG to incorporate stakeholder comments**

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Next Steps

- **Seek an approval vote at the Management Committee on October 30, 2019**
- **Seek Board of Director approval in November**
- **Section 205 Filing at FERC in December**

Questions?

The Mission of the New York Independent System Operator, in collaboration with its stakeholders, is to serve the public interest and provide benefit to consumers by:

- Maintaining and enhancing regional reliability
- Operating open, fair and competitive wholesale electricity markets
- Planning the power system for the future
- Providing factual information to policy makers, stakeholders and investors in the power system



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