UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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Competitive Transmission Development	)	Docket No. AD16-18-000
Technical Conference	)	
	)	
	)	

COMMENTS OF THE INDEPENDENT MARKET MONITOR FOR PJM

Pursuant to the Notice Inviting Post-Technical Conference Comments issued in the above referenced proceeding on August 3, 2016, Monitoring Analytics, LLC, acting in its capacity as the Independent Market Monitor for PJM ("Market Monitor"), offers these comments for the Commission's consideration on issues related to competitive transmission development processes, including the use of cost containment provisions, the relationship of competitive transmission development to transmission incentives, and other ratemaking issues.

I. COMMENTS

A. Cost Containment Provisions

Cost containment provisions in the form of hard cost caps are essential to permit meaningful competition to build transmission projects. Cost caps should be a requirement of all proposals to build transmission projects and not a voluntary element with a weight attached in the evaluation process. Without cost caps, there is no effective incentive to bid competitively. Cost caps must be binding. Cost caps should not include any exceptions. Vague and unenforceable cost caps are not meaningful. Vague and unenforceable cost caps will create an incentive to engage in strategic behavior.

In *Primary Power*, PJM cited lower costs as a basis for its selection but there was and could be no actual support for that position.[1] PJM rules place no limits on the costs recovered by project sponsors, regardless of how they compare to the costs used to evaluate competing alternatives.

Cost caps place the risk of overruns on project developers, the parties most capable of managing such risks. Customers have no ability to manage development risks and should be insulated from such risks.

Cost caps should be required for both incumbent transmission owners and competitors to ensure that the process is competitive. The incumbent transmission owner would be given an overwhelming advantage if it were not also required to offer subject to a cap.

Cost caps should serve as caps and not guarantees. Developers should be required to demonstrate actual costs incurred and be limited to recovery of such costs. All competitors are competing for the opportunity to receive a guaranteed stream of revenues.

At this time, regional transmission system operators should be permitted to develop rules for competitive transmission development for their own regions, subject to Commission guidance on key issues to preserve competition and transparency. The Commission should set up an independent and transparent process for competitive transmission development to govern areas lacking an RTO/ISO.

An independent entity should monitor the transmission procurement process and should monitor and verify compliance with cost containment provisions and actual costs. RTO/ISOs are not sufficiently independent of their transmission owning members to perform this function and there is no effective way to address this conflict of interest while membership in RTO/ISOs remains voluntary.

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[1] 140 FERC ¶ 61,054 at PP 36, 75.

The Commission has accepted proposals to allow incumbent and nonincumbent transmission developers to recover, under certain circumstances, costs associated with developing transmission projects that are proposed but not selected in a regional transmission plan for purposes of cost allocation.

The Commission should not allow recovery of any transmission project costs for projects that are proposed but not selected. This is an essential part of the process of competition.

B. Transmission Incentives and Competitive Transmission Development Processes

Incentive adders for constructing transmission projects should be eliminated. Regulatory determinations of return on investment should be eliminated. Rather than focus on the potential variety of regulatory incentives to transmission companies and the associated increase in costs to customers, the Commission should focus on ways to increase competition and to reduce the cost of transmission to customers. Competition provides an opportunity to allow the market to determine the return necessary to incent project development. Competition can secure needed transmission development at lowest cost. Capital markets are a significant source of increased competition for financing transmission projects.

An important improvement, within the framework defined by Order No. 1000, would be a provision for the competitive procurement of capital. Order No. 1000 explicitly declined to "mandate a competitive bidding process for selecting project developers." PJM can select the projects to develop through the RTEP process without establishing a process for competitive bidding. However, once PJM has selected among proposed projects, PJM should select the source of capital to finance the project based on a competitive process rather than the traditional cost of capital analysis and/or incentive rate approach. There is no reason why the development, construction and management of a transmission facility cannot be separated from financing the facility.

There is no reason that competition to provide capital should not apply for all transmission projects, regardless of size. None of the arguments about why smaller projects or projects at substations or other specific types of projects should not include competition apply to competition to provide capital.

A competitive market can best determine the cost of capital required for a project. This is true for the same reasons that the Commission has introduced regulation through competition elsewhere. Competitive procurement of capital could attract potential nonincumbent participation to provide capital for all projects developed and included in the RTEP. Meanwhile, PJM, with advice from stakeholders and the oversight of the PJM Board, could continue to independently evaluate and select, on the basis of the most transparent criteria possible, the projects that best promote the public interest in obtaining reliable power at least cost. PJM and its stakeholders should continue to look for ways to enhance PJM's independence, objectivity and transparency in making these determinations.

Competitive procurement of capital avoids the issue of who holds title to a project and who constructs a project.

In *Primary Power*, a nonincumbent received preliminary approval for a package of incentives and other elements of a future cost of service filing, subject to future cost of service rate filings and the project's inclusion in the PJM RTEP. That incentive package reflected the Commission's assessment of the "the demonstrable risks or challenges faced by the applicant." With some elements of its rate determined on a preliminary basis, the nonincumbent's task was to ensure that that its project was included in the RTEP with it designated as the sponsor to finance, develop and own the project. In other words, the competition occurred between incumbent transmission owners and nonincumbent transmission owners seeking to stand in the shoes of incumbents. A competition for incumbent status falls short of the benefits a competitive transmission policy could achieve.

If the policy promoting competitive transmission investment emphasized competition to provide capital, the problems related to project identity, upgrades versus new projects, control over physical assets and access to property could be reduced or avoided. Ownership of projects in the sense of title and property access could remain with incumbents even if a nonincumbent financed the project. Competition to construct projects already occurs among the discrete group of firms capable of constructing transmission projects. Competitive financing should have no impact on who actually constructs projects.

The competitive process should select as the project's source of capital the lowest cost supplier of capital. Suppliers of capital would determine their own required returns, and the Commission would avoid the need to make these determinations administratively. The incumbent could compete to provide capital along with any other party.

Competition among suppliers of capital willing to bear investment risks at least cost would allow the Commission to facilitate the robust transmission system that it has determined are needed, at substantially lower cost than would otherwise be possible.

Hard caps on project costs for competitive projects implicitly include competition for cost of capital, which is one of the costs of the project. When such a competitive design is not in place for a procurement, direct and explicit competition to provide capital at least cost would add critical competitive forces to such procurement.

II. CONCLUSION

The Market Monitor respectfully requests that the Commission afford due consideration to these comments as the Commission considers the issues raised in this proceeding.

Respectfully submitted,

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