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ALERT

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FERC Issues Final Rule on Transmission Planning and Cost Allocation Requirements

Introduction

On July 21, 2011, the Federal Energy Regulatory Commission (FERC) issued Order No. 1000, a Final Rulemaking that amends the transmission planning and cost allocation requirements previously established in Order No. 890.¹ In more than 600 pages, FERC adopted requirements that it hopes will have the effect of opening transmission development to competition from independent developers. The Final Rule is already drawing substantial criticism and will likely be subject to rehearing and appeal.

FERC's stated purpose for this rulemaking was to ensure that jurisdictional transmission services are "provided at just and reasonable rates and on a basis that is just and reasonable and not unduly discriminatory or preferential." The Final Order enacts four requirements in pursuit of this goal:

1. That each public utility transmission provider participate in a regional transmission planning process that produces a regional transmission plan;
2. That each public utility transmission provider amend its OATT to describe procedures that provide for the consideration of transmission needs driven by public policy requirements;
3. That the federal right of first refusal for certain new transmission facilities be removed from FERC-approved tariffs; and
4. That coordination between neighboring transmission planning regions be improved to encourage the development of interregional transmission facilities.

In addition, the Final Order concludes that regional transmission planning processes must have a regional cost

allocation method for the cost of new transmission facilities and interregional cost allocation methods for the cost of any new transmission facilities that are located in two or more neighboring planning regions.

As the Commission noted in Order No. 1000, the Final Rule is designed to address inadequacies in the Order No. 890 requirements, which failed to adequately encourage just and reasonable transmission development and cost allocation. For example, Order No. 890 did not require transmission providers to develop regional transmission plans to determine whether certain transmission projects might be more cost effective or efficient than other projects; transmission utilities were not required to consider transmission needs at the local or regional level; non-incumbent transmission developers could be discouraged by incumbent utilities' rights of first refusal to develop transmission facilities (that the order calls "federal rights of first refusal"); and few procedures existed to evaluate interregional transmission solutions.² By enacting the requirements of Order No. 1000, FERC seeks to correct the deficiencies of the former planning process, and achieve its objective of a coordinated, open and transparent transmission planning process.

¹ *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, Order No. 1000, RM10-23-000 (Jul. 21, 2011) at ¶ 1, citing *Preventing Undue Discrimination and Preference in Transmission Service*, Order No. 890, 72 FR 1266 (Mar. 15, 2007), FERC Stats & Regs, ¶ 31,241, *order on reh'g*, Order No. 890-A, 73 FR 2984 (Jan. 16, 2008), FERC Stats & Regs, ¶ 31,261 (2007) *order on reh'g and clarification*, Order No. 890-B, 73 FR 39092 (July 8, 2008), 123 FERC ¶ 61,299 (2008), *order on reh'g*, Order No. 890-C, 74 FR 12540 (Mar. 25, 2009), 126 FERC ¶ 61,228 (2009), *order on clarification*, Order No. 890-D, 74 FR 61511 (Nov. 25, 2009), 129 FERC ¶ 61,126 (2009).

² Order No. 1000 at ¶3.

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Reform Concerning Regional Transmission Planning

In the Notice of Proposed Rulemaking (NOPR), the Commission proposed the requirement that each public utility transmission provider must participate in a regional transmission planning process that satisfies existing Order No. 890 transmission planning principals, and that produces a regional transmission plan.³ Those planning principles are (1) coordination; (2) openness; (3) transparency; (4) information exchange; (5) comparability; (6) dispute resolution; and (7) economic planning studies.⁴ In the Final Rule, the Commission determined that this requirement is necessary to ensure proactive cooperation among public utility transmission providers, which in turn will better identify transmission solutions to more efficiently or cost-effectively meet the reliability needs of regional transmission providers.⁵

In addition to mandating compliance with the seven planning principles set forth in Order No. 890, the Final Rule also requires that each public utility transmission provider amend its OATT to explicitly provide for consideration of transmission needs driven by “Public Policy Requirements” in both local and regional transmission planning processes.⁶ According to the Commission, consideration of such policy requirements would likely facilitate more efficient and cost-effective transmission planning.⁷

Federal Right of First Refusal

In the NOPR, FERC had proposed eliminating the provision that grants incumbent utilities the right of first refusal to construct a proposed transmission project in their service territory.⁸ FERC questioned whether this might result in undue preference to incumbent utilities, and discriminate against non-incumbent utilities that would not get the opportunity to construct transmission facilities in certain areas. This in turn would discourage non-incumbent utilities from participating in the regional transmission process.⁹

After reviewing the comments received during the NOPR process, the Commission determined that incumbent utilities must remove provisions from their Commission-jurisdictional tariffs and agreements that grant them a right of first refusal to construct transmission facilities.¹⁰ These provisions, FERC stated, have the potential to undermine the evaluation of more efficient or cost-effective solutions to regional transmission needs, and lead to rates for transmission service that are unjust and unreasonable. By removing them, FERC will remove a barrier to participation by all potential transmission providers in a given region.¹¹ FERC noted in the Final Rule that the elimination of the federal right of first refusal would apply only to new transmission facilities. Incumbent transmission owners will be permitted to maintain a federal right of first refusal for upgrades to their own transmission facilities.

Interregional Transmission Coordination

In the NOPR, FERC proposed a requirement that each public utility transmission provider, through its regional transmission planning process, (1) develop procedures for sharing information regarding the respective needs of neighboring transmission planning regions; (2) develop and implement procedures for neighboring public utility transmission providers to identify and evaluate transmission facilities that are proposed to be located in both regions; (3) exchange planning data and information between neighboring transmission planning regions at least annually; and (4) maintain a website or e-mail list for the communication of information related to interregional transmission coordination.¹² In the Final Rule, FERC adopted these measures in order to broaden the geographic scope of transmission planning and enable an adequate analysis of the benefits associated with interregional transmission facilities that address transmission needs in an efficient and cost-effective manner.¹³ However, the Commission declined to require a formal planning agreement between public utility transmission providers of neighboring transmission planning regions, as proposed in the NOPR.¹⁴

Proposed Reforms: Cost Allocation

As part of the Final Rule, FERC required that each public utility transmission provider have in its OATT a method or methods for allocating the costs of new transmission facilities selected through the regional transmission plan, and that each public utility transmission provider develop a method for allocating the costs of new interregional transmission facilities.¹⁵ As stated in the NOPR, FERC found that challenges concerning the cost of transmission have become more acute as the need for new transmission infrastructure has grown. However, there are few rate structures currently in place that provide for an analysis of the beneficiaries of a transmission facility, and for the corresponding allocation and recovery of the facility's costs.¹⁶ In enacting this requirement, FERC's goal is to

³ *Notice of Proposed Rulemaking* at ¶ 44.

⁴ Order No. 1000 at ¶ 118.

⁵ *Id.* at ¶¶ 78-79.

⁶ *Id.* at ¶ 203.

⁷ *Id.*

⁸ *Notice of Proposed Rulemaking* at ¶ 89.

⁹ Order No. 1000 at 226.

¹⁰ *Id.*

¹¹ *Id.* at 253.

¹² Order No. 1000 at ¶ 345.

¹³ *Id.* at ¶ 368.

¹⁴ *Id.* at ¶ 475.

¹⁵ Order No. 1000 at ¶ 482.

¹⁶ *Id.* at ¶ 485.

establish a more stable method of transmission cost allocation, and reduce the number of litigated cases related to transmission infrastructure cost allocation.¹⁷

To further these goals, the Commission adopted six “Cost Allocation Principles” that public utility transmission providers’ cost allocation methods must satisfy. The Cost Allocation Principles are as follows:

- Costs must be allocated in a way that is roughly commensurate with benefits;
- No involuntary allocation of costs to non-beneficiaries;
- A benefit-to-cost ratio not to exceed 1.25 unless approved by the Commission;
- Costs must be allocated solely within the benefitting transmission planning region(s), unless those outside the region(s) voluntarily assume costs;
- There must be a transparent method for determining benefits and identifying beneficiaries; and
- Different methods of allocation may be used for different types of facilities.¹⁸

The Final Rule does not stray too far from the principles and requirements set forth in the NOPR. Criticism leveled at the rule revolves around a perceived lack of clarity in its requirements. For example, while the rule requires that costs must be allocated in a way that is roughly commensurate with the benefits, critics point out that the rule has not altered the cost sharing approach that has faced opposition by many industry participants.

Requests for rehearing must be filed with FERC no later than Monday, August 22, 2011.

For more information on the content of this alert, please feel free to contact Theodore F. Duver at 212.407.4158 or tduver@loeb.com or Jay Matson at 202.618.5010 or jmatson@loeb.com.

¹⁷ *Id.* at ¶ 498.

¹⁸ Order No. 1000 at ¶¶ 603-693.

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