

How FERC Is Fueling New Merchant Transmission Projects

Law360, New York (February 27, 2013, 12:45 PM ET) -- On Jan. 17, the Federal Energy Regulatory Commission issued a policy statement providing guidance on the allocation of capacity for new merchant transmission projects and new nonincumbent, cost-based, participant-funded transmission projects.[1] Here, we focus on the new rules that will apply to development of merchant transmission projects. In sum, these rules should help promote additional transmission development, which is a clear goal of FERC.

Unlike traditional utilities, which recover their costs through cost-of-service transmission rates recovered from customers under open-access transmission tariffs, investors in merchant transmission projects assume the risk associated with the projects they develop. To receive the authority to enter into negotiated transmission rates, a merchant transmission project generally was required to allocate transmission capacity using an open season,[2] although a portion of transmission capacity could be allocated pursuant to an anchor customer presubscription.[3]

To provide greater flexibility for new transmission development, FERC stated in the policy statement that it now will permit the following:

- Transmission developers may select a subset of customers (that are based on not unduly discriminatory or preferential criteria) and negotiate directly with those customers to reach agreement on rates, terms and conditions.
- Up to 100 percent of transmission capacity may be allocated through bilateral negotiations, provided that developers broadly solicit interest in the project from potential customers and demonstrate compliance with the solicitation, selection and negotiation process criteria identified in the policy statement.
- Capacity may be allocated to affiliates when done in a transparent manner with adherence to certain protections, including open solicitation.



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FERC will continue to apply the four-factor analysis for evaluating requests by merchant transmission providers for negotiated rate authority. Those four factors are:

- The justness and reasonableness of rates
- The potential for undue discrimination
- The potential for undue preference, including affiliate preference
- Regional reliability and operational efficiency requirements

FERC stated in the policy statement that it will deem the second (undue discrimination) and third (undue preference) factors as satisfied if the merchant developer follows the guidelines in the policy statement. The other two factors remain elements of FERC's analysis of merchant applications for negotiated rate authority.

Transparency of Capacity Allocation

FERC now will permit merchant transmission developers to engage in an open solicitation of interest from potential transmission customers in lieu of the previous requirement of a formal open season. Such open solicitation should include a broad notice that ensures all potential and interested customers are informed of the proposed project (e.g., published in trade magazines or regional energy publications).

Such notice should include transmission developer points of contact, relevant project dates, sufficient technical specifications and contract information including:

- Project size/capacity: MW and/or kV rating (specific value or range of values)
- End points of line (as specific as possible, such as points of interconnection to existing lines and substations)
- Projected construction and/or in-service dates
- Type of line (e.g., AC, DC, bidirectional)
- Precedent agreement (if developed)
- Other capacity allocation arrangements (including how it will address potential oversubscription of capacity)
- Developer's criteria for selecting transmission customers (e.g., credit rating, "first mover" status — customers who respond early and take on greater project risk)
- Customers' willingness to incorporate project risk-sharing into their contracts

Developers can also adopt specific objective criteria that they will use to rank prospective customers so long as they can justify why such criteria are appropriate. In addition, the commission expects the merchant transmission developer to update its posting if there are any material changes to the project's nature or status of the capacity allocation process.

FERC will continue to require merchant transmission developers to disclose the results of their capacity allocation process, but that disclosure will now be noticed and acted upon under Section 205 of the Federal Power Act.

The merchant transmission developer should demonstrate the fairness of its process by providing certain information, such as the criteria used to select customers, any price terms, any risk-sharing terms and any conditions that served as the basis for identifying the transmission customers selected. Specifically, the commission will expect that the developer include, at a minimum, the following information in the demonstration:

- Steps the developer took to provide broad notice, including the project information and customer evaluation criteria that were relayed in the broad notice
- Identity of the parties that expressed interest in the project, placed bids for project capacity, and/or purchased capacity
- Capacity amounts, terms and prices involved in that interest, bid or purchase
- The basis for the developer's decision to prorate, or not to prorate, capacity if a proposed project is oversubscribed
- The basis for the developer's decision not to increase capacity for a proposed project if it is oversubscribed (including the details of the economic, technical or financial infeasibility that is the basis for declining to increase capacity)
- Justification for offering more favorable rates, terms and conditions to certain customers, such as "first movers" or those willing to take on greater project risk-sharing
- Criteria used for distinguishing customers and the method used for evaluating bids
- An explanation of decisions used to select and reject specific customers (the report should identify the facts, including any rates, terms or conditions of agreements unique to individual customers that led to their selection and relevant information about others that led to their rejection).

Discretion as to when to seek FERC approval for its capacity allocation process remains with the developer. For example, a developer can either seek approval of its capacity allocation approach after having completed the process of selecting customers or first seek approval of its capacity allocation approach and then demonstrate in a compliance filing to the FERC that the developer's selection of customers was consistent with the approved selection process.

Under either approach, FERC will notice the filing, allow for protests and reach a determination regarding whether the developer's selection of customers was transparent and not unduly discriminatory or preferential.

Affiliate Participation

With respect to potential affiliate participation in the capacity allocation process, FERC will continue to expect an affirmative showing that the affiliate was not afforded an undue preference. That is, the developer will bear a "high burden" to demonstrate that the assignment of capacity to its affiliate and the corresponding treatment of nonaffiliated potential customers is just, reasonable and not unduly preferential or discriminatory.

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[1] Allocation of Capacity on New Merchant Transmission Projects and New Cost-Based, Participant-Funded Transmission Projects: Priority Rights to New Participant-Funded Transmission, 142 FERC ¶ 61,038 (2013).

[2] E.g., Northeast Utils. Serv. Co., 97 FERC ¶ 61,026 at 61,075 (2001).

[3] Chinook Power Transmission LLC, 126 FERC ¶ 61,134, at P 46 (2009).

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