TAC Options:

Second Revised Straw Proposal

Addendum – Responses to Stakeholder Comments

October 6, 2016

1. Embedded/integrated new PTOs

Stakeholder Comments

In the May 20, 2016 revised straw proposal the ISO proposed to allow a new PTO that is embedded within or electrically integrated with an existing sub-region to have a one-time choice to join that sub-region or become a separate sub-region. Stakeholders commented on whether such an embedded/integrated new PTO should become a new sub-region, be given a one-time choice, or whether another approach would be preferable. Stakeholders were split on allowing a PTO to make a one-time decision to form their own sub-region or join a sub-region.

XES suggested that existing sub-regions should make the decision rather than the new PTO. In the case of disputes, FERC would determine the terms of the integration. Many stakeholders expressed concern for cost shifts that would occur unless there was an agreement by both the existing sub-region and the new PTO. Specifically, WRA stated that "A small PTO joining a large sub-region would have minimal effect, while a larger PTO in a smaller sub-region might." SCE recommended the creation of geographic based sub-regions upfront and before any new non-California based PTOs join the ISO. The sub-regions need to be large enough to contain multiple utilities that currently benefit from each other's transmission assets, but not so large that it would be difficult to justify benefits are shared among the utilities within the geographic sub-region.

Several stakeholders were not clear on the details of what it means to be electrically integrated. IID expressed concern over the ISO's proposal at the August 11, 2016 working group to no longer allow embedded entities a one-time option. SMUD requested, "confirmation that a new PTO that is "electrically integrated" with an existing sub-region is still provided a one-time option upon joining to elect to retain its own transmission rate or choose the transmission rate of the neighboring sub-region."

ISO Response

The ISO has proposed that once the first PTO joins, the expanded ISO BAA will become the new "region" consistent with Order 1000. The current CAISO system would be considered a "sub-region," as would the first PTO and each subsequent new PTO with a load service territory that joins, unless the new PTO is embedded within or electrically integrated with an existing sub-region. The ISO now proposes that a new PTO that is embedded within an existing sub-region would join that sub-region. In the case of a new PTO electrically integrated with an existing sub-region, the ISO proposes a case-by-case decision process based on specific criteria to determine whether the new PTO should join the existing sub-region.

The ISO proposes to define "embedded" to mean that the new PTO cannot import power needed to serve its load into its service area without relying on the transmission facilities of an existing sub-region. In response to SMUD's request, the ISO clarifies that "integrated" at a minimum means that the new PTO is not entirely dependent – perhaps not dependent at all – on another PTO's transmission facilities to import energy prior to joining, but once it joins the expanded BAA it will benefit significantly from the transmission system of the sub-region with which it is integrated. Rather than establish a precise definition of "integrated," the ISO proposes to make this determination on a case-by-case basis, subject in each case to the approval of the Board of Governors for the expanded BAA, and considering specific criteria stated in the tariff such as the proportion of the new PTO's annual and peak load served over the

facilities of the existing sub-region and the existing tariff criteria for defining an "integrated BAA." Although there were some stakeholders in support of a one time decision for a new PTO to choose to be their own sub-region or join an existing sub-region, the ISO believes that, based on the proposed definition of embedded, it is not appropriate to allow such an entity to form its own sub-region. Rather, providing clear definition of an "embedded" PTO, plus criteria for assessing "integrated" and allowing for a case-by-case approval by the ISO Board of Governors will allow for a transparent process that will consider the various impacts and benefits to both the existing sub-region and a new PTO.

In response to SCE's comment, the ISO believes that defining geographic/electrical sub-regions across the west is beyond the scope of this initiative.

2. Existing facilities

Stakeholder Comments

The May 20 revised straw proposal defined existing facilities as transmission assets in-service or planned in the entity's own planning process for its own service area or planning region, and that have either begun construction or have committed funding. The ISO proposed criteria for what constitutes a facility having "begun construction" and "committed funding" and for how these criteria would be demonstrated. In the 2nd revised straw proposal the ISO has simplified its proposal to determine that "existing facilities" are any transmission elements that are not planned and approved via an integrated Transmission Planning Process (TPP). UAMPS suggested that the term existing facilities be more specific and only apply to facilities that are in service and in a PTO's rate base at the time of formation of the Regional ISO. SDG&E agreed with the ISO by defining new facilities as transmission facilities that are approved for cost recovery through the expanded ISO's TPP and every other transmission facility would be considered an existing facility for purposes of cost recovery.

Stakeholders also suggested that for facilities that are in development, a new class of facilities would be defined and would be analyzed on a case-by-case basis. These could be called transitional facilities. Because the timing of the development of new major transmission spans so many years, from first permitting efforts to construction, it is difficult to lump all projects into one category.

PG&E expressed concern that existing facility costs will not be shared on a regional basis despite the benefits to the broader region provided by existing facilities. And if existing facility costs will not be shared regionally, then regional allocation of new facility costs should be limited. ORA and SVP also propose that existing transmission costs should be allocated to all sub-regions in the expanded ISO based on the benefits received from existing facilities.

ISO Response

In response to stakeholders, the ISO has proposed a bright line between an existing facility and a new facility based on whether it was planned through the integrated TPP for the expanded ISO ("new") or not ("existing"). In response to UAMPS' and others' proposal to create a 'transitional' category, the ISO notes that such projects would have been planned and approved within one sub-region's planning process to meet the needs of that sub-region, which conflicts with the principle the ISO is now proposing that facilities eligible for regional cost allocation should be planned and approved in an integrated TPP

that includes all stakeholders for the expanded BAA. In response to PG&E and other stakeholders' concerns of not blending existing facility costs, the ISO has considered alternative ways to carve out a subset of existing facilities for this purpose and ultimately concluded that any such provisions would be arbitrary and controversial, and the complexities and risks of such an approach would be counterproductive. In approving license plate rates for existing facilities in the context of other ISOs/RTOs, FERC has accepted that the individual PTO areas had made decisions to build their existing systems for the benefit of their existing ratepayers without any anticipation of some other parties paying part of those costs. Keeping the existing facility costs separate means that no area experiences a positive or negative rate impact that would occur if costs of some existing transmission facilities were merged and reallocated.

3. New facilities

Stakeholder Comments

"New facilities" or "new transmission facilities" are transmission elements that are planned and approved via an integrated TPP for the expanded ISO BAA. The "new facilities" category could include a project that was being considered prior to the new PTO joining the ISO as an "inter-regional" project under the FERC Order 1000 approved provisions for considering inter-regional transmission projects, and then is subsequently adopted and approved via the integrated TPP. Stakeholders provided a variety of comments that ranged from the three categories of projects to whether a recalculation of cost allocation is necessary.

BPA notes that they are opposed to the proposal of a benefits recalculation for new facilities every 5-years. They note that this has the potential of creating instability in the rates process, does not provide certainty, and may lead to rate shock. They also note that only those facilities that are directly impacted by the addition of the new PTO should undergo recalculation. The UOCS believes that there should be a transition period for cost allocation of new transmission projects. The cost of projects (reliability, policy or economic) built for one sub-region should be allocated entirely to that sub-region for a certain number of years. PG&E recommends that the only project that should be eligible for cost allocation to multiple sub-regions are ones that interconnect two sub-regions or connect the expanded ISO BAA with a neighboring BAA.

Reliability projects

PG&E and CLECA support that projects that are solely needed for reliability should be fully allocated to sub-region(s) with reliability concerns. In combined projects, the portion of costs attributable to reliability concerns should first be allocated to sub-regions according to reliability benefits. CLECA also recommends making the reliability assessment and cost allocation first prior to parsing economic costs and benefits.

Other stakeholders including TransCanyon and ICNU do not support a full allocation to a sub-region for reliability projects. Their main idea is that all reliability projects will provide a mix of benefits. Stakeholders in support of this notion believe that it is necessary to allocate costs in proportion to the benefits each sub-region receives.

Economic projects

PG&E, ICNU, LS Power, and ORA support an approach where projects that are justified on economic grounds will be fully allocated to sub-region(s) with economic benefits according to TEAM. In combined projects, reliability allocation should come first, then the portion of costs attributable to economic goals should be allocated to sub-regions according to economic benefits based on TEAM. Clean Coalition believes that if costs related to non-economic needs are allocated first, then this can create undue windfall profits and disproportionate distribution of economic benefits.

Policy projects

A majority of stakeholders agreed with the proposal that the Western States Committee (WSC) would determine if a policy project would be built along with the cost allocation. But those who opposed believed that information revolving around the structure and process of the WSC was too vague to support the proposal.

UOCS believes that, "if a state's policy is driving the need for a project, then that state should initially be responsible for all the costs of the project. Once the project is in-service and actual benefits can be measured, then it would be appropriate to ask other states to share in the costs based on the benefits achieved. However, no non-policy state should have to bear any costs that exceed its benefits."

TEAM

PG&E and SVP support comprehensive reevaluation of TEAM methodology, with some proposing a separate stakeholder initiative. SVP believes that the TEAM methodology should be applied only to allocating costs associated with reliability and economic projects and not for policy projects. UAMPS believes that the TEAM document should be evaluated to see if it is applicable to a broader footprint and whether it could apply to PacifiCorp's process of planning on a contract path basis. SCE suggested that "for cost allocation between regions, there needs to be more investigation if the TEAM needs to be modified to include benefits to producers and the regional economy." Essentially, as part of the benefits analysis in the regional context, SCE is suggesting to add factors such as benefits to producers and region-wide economy. ICNU and the UOCS expressed concern about inclusion of resource adequacy capacity costs in TEAM calculation.

Stakeholders requested that the ISO add the following benefits to a TEAM/benefits assessment:

1. Avoided costs alone are not adequate. With reference to SPP staff analysis benefits considered should include avoided or delayed reliability projects, reduced loss of load probability, capacity cost savings due to reduced on-peak transmission losses, access to lower cost generation resources (AWEA), and avoided costs for facilities that otherwise would be necessary to maintain reliability (Six Cities)
2. Costs which can reasonably be expected to be avoided by the prospective transmission upgrade should be included in the benefits for cost allocation purposes. (SDG&E)
3. Benefits associated with the avoided costs of alternative reliability or public policy projects, reduced emissions, as well as operating reserves benefits and reduced costs of renewable resource integration and curtailment (TransCanyon)
4. Hurdle rates, dynamic path limits, other base assumptions, market dynamics, and sub-hourly economic benefits (LS Power)

5. Economic multiplier benefits that accrue to a region that produces energy (such as job creation and increased tax revenue) and greenhouse gas emissions cost savings (ORA)
6. Indirect benefits of a transmission upgrade, such as increased economic activity and increases in employment, should be evaluated at least qualitatively. (SDG&E)
7. Emission reduction benefits as envisioned in the original TEAM (SVP)
8. All economically derived benefits associated with transmission investment, including benefits associated with accessing lower-cost resources whether they are for resource adequacy, lower economic dispatch and/or RPS requirements (TransWest)

Stakeholders also commented on the possibility of an avoided cost element in TEAM. TransWest believes that the avoided costs should be used only for reliability projects. Clean Coalition commented that while considering avoided costs, the ISO should consider all alternatives, including non-transmission alternatives. LS Power and UOCS were cautious about the use of speculative hypothetical alternatives. SDG&E believes that it is important to define a reference case that represents a realistic view of what would be done in the expanded ISO footprint if a proposed transmission upgrade were not built. But CLECA and SCE believe that it is difficult to take a position on the use of avoided costs in allocation without more detail on how avoided costs would be used for cost allocation.

The UOCS requested that the ISO present how benefits are quantified in each major U.S. ISO/RTO's economic planning and/or cost allocation processes as well as in the other western planning regions (NTTG, ColumbiaGrid, WestConnect) and compare the ISO's proposal.

ISO Response

The ISO's second revised straw proposal reflects many comments that were submitted by stakeholders. BPA's comment on the recalculation of cost allocation were consistent with the view of multiple stakeholders who were concerned of the uncertainty revolving future cost exposures. The ISO has responded and dropped the proposal to recalculate the benefits of new transmission facilities. The ISO has concluded that the request for a transitional rate period for new transmission facilities to avoid rate shock does not take into account that new facilities will undergo a regional TPP that will take into account benefits to a sub-region and reflect cost allocation based on the benefits assessment. In response to PG&E's recommendation to limit region-wide cost allocation to projects that interconnect sub-regions or connect to a neighboring BAA, the ISO believes that this criterion would be too limiting in that other projects will likely provide benefits to more than one sub-region.

In response to ICNU and TransCanyon's comments on reliability projects, the ISO recognizes that a reliability-driven project that is approved solely to meet an identified reliability need within a sub-region may provide incidental benefits to another sub-region, but the project would not be built but for the reliability need and therefore the cost should be allocated entirely to the sub-region whose reliability need was the driver of the project.

In response to the comments that the TEAM methodology include the economic benefits of increased generation or economic development including possible employment and other benefits, the ISO considers that expanding economic benefits beyond the direct economic benefits of the ratepayers that would fund the development is practically unworkable as a cost allocation mechanism. Besides being extremely difficult to develop a consensus approach to determining which benefits to include and how to measure them, especially when they would be used as the basis of costs applied to ratepayers, these

benefits become indistinguishable at some point from policy drivers established for policy driven transmission.

Similarly, in response to TransWest's comment that economic benefits should include the economic benefit of alternative means of achieving policy direction, the ISO is concerned that in many cases well-defined alternative means to achieve policy objectives many not exist to provide credible estimates of avoided cost benefits. For this reason the ISO is now proposing relatively simple default provisions for policy-driven projects that benefit more than one sub-region, in anticipation of a likely role for a new Western States Committee in this area.

In response to CLECA and SCE, the ISO has identified specific scenarios where avoided costs would be used. When a reliability or policy-driven project is enhanced or replaced by a more costly project that also provides economic benefits that exceed the incremental cost above the cost of the original reliability or policy-driven project, the avoided cost of the original project will first be allocated to the sub-region with the original reliability or policy need, and the incremental cost will be allocated to sub-regions in proportion to each sub-region's benefits.

In response to UOCS' request for a review of benefits calculations in each major U.S. ISO/RTO, the ISO presented in the March 1, 2016 meeting a comparison of ISO/RTO benefits calculation for policy projects as well as proposed alternative assessments such as DFAX.

4. Region-wide export charge

Stakeholder Comments

A majority of stakeholders supported the proposal for a single, region-wide, export charge. Specifically, SCE commented that the single rate has the advantage of not creating market and system distortions by external parties attempting to exploit locations with a cheaper transmission charge. Additionally, AWEA believes that a single charge should help to reduce overall seams issues in the long-run.

BPA, UAMPS, and PAC do not support a region-wide access charge for exports, and contend that there is a better option than the load-weighted average proposal. BPA suggests that the ISO should set an EAC less than or equal to the lowest sub-regional TAC rate, so that customers exporting energy out of any sub-region would not have to pay a higher EAC rate than the sub-region's TAC. In addition, they note that with a lower EAC rate external entities would have an incentive, under the BPA approach, to export excess power out of the CAISO during periods of oversupply. BPA also expressed concern that the weighted average EAC rate would result in PAC or possibly other PTOs over-collecting on their TRRs. PAC argues that blending the WAC would result in inappropriate cost shifts to PAC customers. They also note that it is not clear why a single WAC (export rate) is reasonable but the TAC structure is based on a different cost-benefit alignment.

ISO Response

In response to BPA, PG&E, and other stakeholders who remained split on the EAC rate, one objective of the ISO's proposal is to achieve a reasonable balance in revenue collection between external entities exporting or wheeling through and internal entities with the TAC. In response to PAC's concern over a single WAC rate, the ISO's rationale for the EAC is that having a different export rate for each sub-region

would create incentives for parties who export from and wheel through the expanded ISO to distort their normal scheduling patterns and thereby cause inefficient grid congestion by seeking to export from the sub-region where the export rate is lowest. The proposal for a single region-wide export rate is consistent with the practices of other multi-state ISOs and RTOs.

Regarding potential over-collection of TRR, this would not be possible because the PTOs use balancing accounts that track their revenues from internal load and exports and will be used to adjust rates to ensure that the correct amount of money is collected each year. However, while it is true that the proposed region-wide EAC rate would not result in over- or under-collection of TRR, it is possible that changes in export volumes and patterns could shift some of the cost recovery between exports and internal load. This is a primary reason why the ISO proposes to use a weighted average of the TAC rates to calculate the EAC rate, rather than an extremely high or low EAC rate. If the EAC rate is too high or too low it could have a greater impact on the volume of exports and the total revenues collected from exports. In response to concerns expressed about the method presented in the August 11 working group for allocation of EAC revenues, the ISO now proposes a revenue allocation method based on each sub-region's high-voltage TRR.