



Memorandum

To: ISO Board of Governors

From: Keith Casey, Vice President, Market & Infrastructure Development

Date: March 8, 2017

Re: Decision on Generator Interconnection Driven Network Upgrade Cost Recovery Proposal

This memorandum requires Board action.

EXECUTIVE SUMMARY

Current rules on recovering costs for network upgrades that are needed to interconnect new generation have become problematic for Valley Electric Association (VEA), and could become problematic for future small transmission owners. These rules require that the cost of generation interconnection-driven network upgrades on a participating transmission owner's (PTO) low-voltage (below 200kV) transmission are to be recovered by that specific PTO's low-voltage transmission access charge. This will have a large adverse impact on VEA's ratepayers where there are significant network upgrade costs spread across a small number of ratepayers who ultimately do not benefit from the generation-driven upgrades. It could be equally problematic for any future similarly situated small PTO as well.

Management's proposal narrowly addresses small PTOs that do not need to procure energy from the generators interconnecting in their area but are nevertheless facing large low-voltage TAC increases due to generator interconnections. The proposal specifies three criteria that will identify whether a PTO would qualify for separate rate treatment that would allow them to put the cost of interconnection-driven low-voltage upgrades into the ISO's high-voltage TAC:

1. Small PTOs, where the PTO's filed annual gross load is 2,000 GWh or less (which currently is approximately 2.2% of the largest PTO's filed annual gross load);
2. The small PTO is in a renewable resource-rich area that is leading to generator regional procurement interest within the area; and

3. The small PTO is not under a Renewable Portfolio Standard (RPS) requirement or, if under an RPS requirement, does not have a need for the new interconnecting generation to meet that requirement.

Consideration of a PTO for separate rate treatment would be performed on a case-by-case basis. ISO Management would propose the PTO for such rate treatment to stakeholders and for ISO Board of Governors approval, and then Federal Energy Regulatory Commission (FERC) approval. Those approved PTOs would then be allowed to put the cost of interconnection-driven low-voltage upgrades into their high-voltage TAC rates.

Management recommends the following motion:

Moved, that the ISO Board of Governors approves the proposal for generator-interconnection-driven network upgrade cost recovery, as described in the memorandum dated March 8, 2017; and

Moved, that the ISO Board of Governors approves Management's determination that Valley Electric Association meets the criteria set forth in that proposal; and

Moved, that the ISO Board of Governors authorizes Management to make all necessary and appropriate filings with the Federal Energy Regulatory Commission to implement the proposed tariff change.

DISCUSSION AND ANALYSIS

The tariff requires PTOs to reimburse interconnection customers in their systems for the costs of reliability¹ and local deliverability network upgrades necessary for the interconnection. The PTOs then include those network upgrade reimbursement costs in their FERC-approved rate bases, requiring ratepayers to pay those costs through either low- or high-voltage TAC. Network upgrades 200 kV and above are considered high-voltage and their costs are recovered through the high-voltage TAC using an ISO system-wide "postage stamp" rate based on the aggregated high-voltage transmission revenue requirements of all PTOs in the ISO system. In contrast, upgrades below 200 kV are considered low-voltage and their costs are recovered through PTO-specific low-voltage TAC rates charged only to customers within the service area of the PTO.

The ISO held a stakeholder initiative to address the concern that the current practice for low-voltage upgrades could negatively impact ratepayers who are not the beneficiaries of the upgrades, but who solely bear their costs. For example, if a large generator or a large number of generators with significant low-voltage network upgrade costs interconnect to a PTO with a relatively small rate base, that PTO's low-voltage transmission revenue requirement and its low-voltage TAC rates may increase

¹ Reimbursement for reliability network upgrades is limited to \$60,000 per installed MW of capacity; there is no limit on reimbursement for costs of local delivery network upgrades.

significantly under the current cost allocation framework, even though the upgrades and the associated generation capacity may not materially benefit or be needed by that PTO's ratepayers. This issue is currently facing VEA where larger-scale renewable generation is seeking to connect to VEA's low-voltage transmission system, driving low-voltage network upgrades that will have a direct adverse impact to VEA ratepayers,² yet the generation is not needed by VEA's ratepayers and is wholly contracting to entities outside of the VEA service territory.

Management's proposed solution is that PTOs, evaluated and approved on a case-by-case basis, that meet the criteria below would have the costs of generator-interconnection-driven network upgrades placed into the regional high-voltage TAC instead of that PTO's local low-voltage TAC. The proposed criteria are:

1. Small PTO, where the PTO's filed annual gross load is 2,000 GWh or less (which currently is approximately 2.2% of the largest PTO's filed annual gross load);
2. The small PTO is in a renewable resource-rich area that is leading to generator regional procurement interest within the area; and
3. The small PTO is not under a Renewable Portfolio Standard (RPS) or equivalent requirement or, if under an RPS or equivalent requirement, does not have a need for the new interconnecting generation to meet that requirement.

However, even where a small PTO meets this criterion and the Board of Governors and FERC agree that it may otherwise qualify for separate rate treatment, if the small PTO's own procurement triggers the needs for network upgrades on its low-voltage system, the cost of those network upgrades will remain in its low-voltage local TAC rate. Also, if a small PTO's situation changes such that it fails to meet any one of the three criteria above, it would cease to qualify for this TAC rate treatment. At that time, any low-voltage network costs stemming from new generator interconnections, as well as any as-yet unrecovered low-voltage costs, would be applied to the PTO's low-voltage TAC rates. VEA or a similarly situated PTO would be required to certify to the ISO annually that they still meet the three qualifying criteria to continue to receive this TAC rate treatment.

² If generation connecting to VEA's low-voltage transmission system drives \$10M in low-voltage network upgrades, VEA's low-voltage transmission revenue requirement would increase by approximately 37.5%. This requirement, combined with their high-voltage transmission revenue requirement, would result in a combined transmission revenue requirement increase of approximately 14%. Alternatively, if VEA could put these costs in their high-voltage transmission revenue requirement, and therefore enable it to be shared among all PTOs, the combined transmission revenue requirement would increase by approximately 0.02-0.06% for each PTO.

POSITIONS OF THE PARTIES

The ISO issued four papers through this initiative. The Issue Paper/Draft Straw Proposal set out a broad range of alternatives. Based on stakeholder input that tended to be polarized advocating one extreme or another, the Revised Straw Proposal focused on a single option from the original issue paper, referred to as Option 1. Option 1 proposed to include the cost of generator-driven low-voltage facilities of *all* PTOs in the aggregated high-voltage transmission revenue requirement for recovery through the system-wide “postage stamp” high-voltage TAC. The Option 1 proposal was polarizing for stakeholders, with some strongly in favor and some strongly opposed.

To gain stronger consensus, and as suggested by a few stakeholders, the Second Revised Straw Proposal and Draft Final Proposal offered the more narrowly focused solution described in this memo. While this proposal gained a majority of stakeholder support, some stakeholders oppose the proposal for various reasons that are described and responded to in the attached stakeholder matrix.

CONCLUSION

Management recommends and seeks Board approval for this proposal. Under the current rules, ratepayers of VEA and any future similarly situated PTO will see significant rate increases for generation being developed in their service territory that does not serve the needs of those ratepayers. Timely resolution is critical because there is a generation interconnection customer in the generation interconnection agreement negotiation phase that requires significant network upgrades to the VEA low-voltage system.