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SWALLOWING THE RULE: WHY FERC'S "IMMEDIATE NEED EXEMPTION" FRUSTRATES COMPETITIVE AND CLIMATE-SMART ELECTRICITY SECTOR TRANSMISSION PLANNING UNDER ORDER No. 1000

*By Philip Killeen**

Last year, the Federal Energy Regulatory Commission (FERC) commendably initiated an investigation into whether three regional transmission organizations (RTOs) were improperly supervising the electrical grid infrastructure development process.¹ ISO-New England (ISO-NE), PJM Interconnection (PJM), and Southwest Power Pool (SPP) (collectively, the "Investigation Subjects") are misusing the narrow "Immediate Need Exemption" ("INE") to standard competitive bidding processes for electricity transmission infrastructure planning in a manner that rewards inefficient and expensive projects at the cost of innovative and climate smart solutions. This Article argues that the Investigation Subjects' use of INE is inconsistent with FERC's duties under the Federal Power Act (FPA)² to ensure just and reasonable—and not unduly discriminatory—rates and practices in interstate transmission markets. This is because INE foregoes substantial consumer savings, unnecessarily restricts new developers from participating in competitive project solicitations, and frustrates states' legitimate policy preferences for reducing electricity sector GHG emissions.

BACKGROUND

Congress enacted the FPA in 1935, vesting FERC with authority to regulate the wholesale sale and transmission of electricity in interstate commerce.³ Pursuant to this authority, FERC was tasked with ensuring all rates received by public utilities for the transmission or sale of electricity under its jurisdiction (and all regulations affecting such rates) be "just and reasonable" and not "grant any undue preference or advantage" or "maintain any unreasonable differences in rates, charges, service, facilities . . . between localities or . . . classes of service."⁴

FERC initially fulfilled this mandate by granting electrical utilities monopoly franchises to generate, transmit, and distribute electricity to a captive customer base in return for a guaranteed rate of return based on their cost of service.⁵ This initial approach allowed utilities to unnecessarily maximize investments in grid infrastructure to ensure a higher guaranteed rate of return based on their cost-of-service.⁶ Recognizing this trend, FERC introduced a series of Orders beginning in the late 20th century, predicated on the understanding that elements of the electricity sector could achieve more efficient (and therefore more "just and reasonable") outcomes for consumers by introducing new technologies and competition.⁷

One such example is Order No. 1000.⁸ The Order introduced three new requirements for transmission planning: (1) each public utility transmission provider must join a transmission planning

region that proactively identifies the need for transmission on a region wide basis;⁹ (2) such transmission planning regions must identify and plan for transmission needs driven by public policy, including the climate-related priorities of the states in which the individual utilities are located;¹⁰ and (3) neighboring transmission planning regions must "coordinate" with each other to evaluate whether interregional transmission facilities could more efficiently or cost-effectively address identified transmission needs.¹¹ Acknowledging that new developers may be more capable of providing these solutions than incumbent utilities, FERC also stipulated that public utility transmission providers must remove from their tariffs any "federal right of first refusal," which grants an incumbent utility the right to build any new transmission facilities called for in regional transmission planning.¹² In so doing, FERC explicitly sought to foster competition between incumbents and new developers in soliciting bids for transmission infrastructure projects called for in regional planning.¹³

Unfortunately, however, these benefits are undermined by INE—an exception threatening to swallow the rule prohibiting the incumbents' right of first refusal for transmission projects. In their Order No. 1000 compliance filings, the Investigation Subjects each proposed a "limited exemption for immediate need reliability projects," whereby an RTO would be given discretion to determine whether there is sufficient time for a transmission project called for in its regional transmission planning to be competitively awarded.¹⁴ By approving these proposals, FERC created a class of transmission projects to be built by incumbent transmission developers that were exempt from the competitive bidding project solicitation process.¹⁵ This decision balanced the fact that INE would act as a barrier to potentially competitive transmission resources provided by new developers and that "it is not in the economic self-interest" of incumbent utilities to expand transmission infrastructure to permit access to competing sources of supply.¹⁶ On the other hand, FERC recognized potential delays in the competitive bidding process for transmission projects could adversely affect an RTO's ability to ensure grid reliability.¹⁷

1. AS APPLIED, INE IS UNJUST AND UNREASONABLE BECAUSE IT FOREGOES SUBSTANTIAL CONSUMER SAVINGS

Eight years of experience with INE demonstrates that FERC has not appropriately balanced reliability concerns with

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consumer costs. Since implementation of Order 1000, RTOs have invested approximately \$17 billion per year in transmission investments, with annual investment growth ranging from 10–16%.¹⁸ However, as a result of INE, RTOs have completed only thirty-one competitive transmission project solicitations, merely twenty-one of which have actually resulted in competitive projects.¹⁹ Put differently, 97% of all FERC-jurisdictional transmission investments occur outside the competitive process in which new developers may compete.²⁰

Research suggests increased use of competitive transmission project solicitations could reduce investment costs by an estimated 25% while increasing investment cost-effectiveness.²¹ To date, the average cost of transmission project proposals selected in competitive solicitations fell 40% below the initial project cost estimates prepared by ISOs and RTOs and the lowest cost offers from incumbent transmission developers.²² By capitalizing on these lower project costs, RTOs could save electricity consumers \$8 billion over five years.²³

2. INE IS UNDULY DISCRIMINATORY BECAUSE ITS ELIGIBILITY CRITERIA UNNECESSARILY RESTRICTS NEW DEVELOPERS FROM PARTICIPATING IN COMPETITIVE PROJECT SOLICITATIONS

To ensure that INE was used only in limited circumstances, FERC established criteria limiting a RTO's discretion to grant the exemption; the most important of which required the project to be needed within three years to resolve the reliability concern.²⁴ FERC determined that the appropriate date to calculate whether a transmission project qualifies for INE is the date that the reliability need must be *addressed*, rather than the date when the project is actually *in-service*.²⁵

This three-year criterion has been applied as a rubber stamp in the Investigation Subjects' markets, allowing incumbent transmission developers to circumvent competitive project solicitations. Since implementation of Order No. 1000, all thirty of ISO-NE's transmission projects were designated as needed for grid reliability within the next three years.²⁶ Accordingly, each qualified for INE and was awarded to incumbent transmission developers without a competitive solicitation.²⁷ However, of these thirty projects, twenty-four (80%) were not in-service within three years.²⁸ Similarly, SPP designated a project for INE in 2018 based on its determination that the project was "needed" by 2020, yet had an expected in-service date in 2023.²⁹ Meanwhile, none of SPP's other INE projects have gone in to service, including those with "need-by" dates in the past.³⁰ Finally, of the thirty-nine transmission projects designated by PJM for INE in 2014, only 72% have gone into service within three years of their "need-by" dates.³¹

The fact that so many transmission projects in these regions qualify as time-sensitive, yet not sensitive enough to *actually be built on time*, suggests that incumbent transmission developers are not using INE to ensure grid reliability, but rather as an anti-competitive measure preventing the participation of new developers. The "immediate need" of these projects is

further undermined by the RTOs' repeated assertions that their grids continue to operate reliably with existing transmission infrastructure.³²

3. INE VIOLATES THE FPA BECAUSE IT FRUSTRATES STATES' LEGITIMATE POLICY PREFERENCE FOR LOW EMISSIONS ELECTRICITY GENERATION

Order No. 1000 requires RTOs to proactively identify and plan for region wide transmission needs driven by public policy.³³ This, FERC concludes, will help ensure that the rates, terms, and conditions for wholesale sales and transmission of electricity are just and reasonable and not unduly discriminatory against stakeholders unrepresented among incumbent utilities.³⁴ Many states are seeking to reduce electricity sector greenhouse gas (GHG) emissions by implementing Renewable Portfolio Standard ("RPS") policies that seek to transition from fossil fuel to renewable-based electricity generation.³⁵ In ISO-NE, each constituent state has implemented RPS policies, with 2020 targets ranging from 10% to 59% of electricity supplied from renewable energy.³⁶ Washington, D.C. and ten of the thirteen states comprising PJM's membership have implemented RPS programs.³⁷ Finally, nine of SPP's fourteen member states have also implemented RPS programs.³⁸

Eliminating the federal right of first refusal serves states' RPS policies because it forces RTOs to consider proposals from new developers that provide ancillary environmental benefits. FERC's definition of new (or "nonincumbent") transmission developers includes entities that propose transmission projects outside of their existing retail distribution service territory or that lack a distribution service territory altogether.³⁹ A transmission project developer from a neighboring RTO and an owner of battery storage infrastructure that is capable of providing transmission services would therefore both qualify as "nonincumbent" transmission developers.⁴⁰

Regionally interconnected transmission networks and battery storage technologies are particularly important for variable renewable energy resources because they transmit electricity between different markets and help diversify a region's resource mix, helping address some of the challenges associated with intermittency and curtailment.⁴¹ With a nationally interconnected grid, the United States could reduce power sector GHG emissions by 80% relative to 1990 levels through renewable energy and natural gas without the need for battery storage or an increase in the levelized cost of electricity.⁴² Most importantly, regionally interconnected transmission markets allow states to source in-state electricity consumption from renewable energy, and thereby meet RPS targets, when intrastate generation facilities are otherwise insufficient.⁴³ However, because INE has substantially frustrated the ability of these new developers to participate in transmission infrastructure planning, it effectively negates FERC's intent in Order No. 1000 to facilitate state public policy goals in the electricity sector. 🌱

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