

December 17, 2019

By Electronic Delivery

Honorable Kimberly D. Bose, Secretary
Federal Energy Regulatory Commission
888 First Street, NE
Washington, DC 20426

Re: New York Independent System Operator, Inc., Proposed Tariff Revisions
Regarding Cost Containment in the Public Policy Transmission Planning Process;
Docket No. ER20-____-000

Dear Ms. Bose:

Pursuant to Section 205 of the Federal Power Act (“FPA”),¹ the New York Independent System Operator, Inc. (“NYISO”) hereby submits, for the consideration of the Federal Energy Regulatory Commission (“the Commission” or “FERC”), proposed revisions to Attachment Y and Rate Schedule 10 of its Open Access Transmission Tariff (“OATT”) to establish procedures providing for the consideration of cost containment in proposed Public Policy Transmission Projects in its Public Policy Transmission Planning Process (“Public Policy Process”).²

The NYISO’s proposed tariff revisions establish cost containment mechanisms that Developers may voluntarily include as part of their proposed transmission projects in the Public Policy Process. The revisions also set forth the manner in which the NYISO will assess these cost containment mechanisms when evaluating proposed transmission solutions and selecting the more efficient or cost effective transmission solution to address a Public Policy Transmission Need. Finally, the revisions establish how the cost containment mechanisms will be implemented as part of the selected project’s cost recovery.

The NYISO developed cost containment provisions for its Public Policy Process to prepare for potential Public Policy Transmission Needs in the current and next cycles of the Public Policy Process.³ The NYISO intends to address cost containment in its reliability and economic planning processes next year.⁴ The NYISO’s stakeholder Management Committee

¹ 16 U.S.C. § 824d (2014).

² Capitalized terms that are not defined in this filing letter shall have the meaning specified in Attachment Y of the OATT, and, if not defined therein, in the OATT or the Market Administration and Control Area Services Tariff (“Services Tariff”).

³ The Public Policy Process requirements are located in OATT Section 31.4.

⁴ The NYISO’s reliability and economic planning processes are located in OATT Sections 31.2 and 31.3, respectively. Stakeholders supported the NYISO establishing cost containment provisions that focus on Public Policy Process first because that planning process has been the most active process in New York in identifying needs and selecting transmission solutions.

approved the tariff changes unanimously with one abstention, and its Board of Directors approved the tariff changes for filing with the Commission.

The NYISO respectfully requests that the tariff revisions proposed in this filing become effective the day immediately following the end of the statutory sixty-day notice period under FPA Section 205 (*i.e.*, February 16, 2020). Upon acceptance by the Commission, the NYISO will apply the tariff changes in the current and future cycles of the Public Policy Process to address new Public Policy Transmission Needs in New York State.

I. DOCUMENTS SUBMITTED

The NYISO submits the following documents with this filing letter:

- Affidavit of Lorenzo P. Seirup, Supervisor of Market Mitigation and Analysis (Attachment I);
- A clean version of the proposed revisions to the OATT (Attachment II); and
- A blacklined version of the proposed revisions to the OATT (Attachment III).

II. COMMUNICATIONS AND CORRESPONDENCE⁵

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⁵ The NYISO respectfully requests waiver of 18 C.F.R. § 385.203(b) (3) (2014) to permit service on counsel in multiple locations.

III. BACKGROUND

The NYISO's Public Policy Process is part of its Comprehensive System Planning Process prescribed in Attachment Y of the OATT. In the Public Policy Process, stakeholders and the NYISO may propose, and the New York Public Service Commission ("NYPSC") identifies,⁶ Public Policy Transmission Needs driven by one or more Public Policy Requirements.⁷ If needs are identified, the NYISO solicits interested Developers to propose solutions to address those needs, assesses which of the solutions are viable and sufficient, and evaluates and selects the more efficient or cost effective transmission solution to address the needs. The Developer of the selected project enters into a Development Agreement with the NYISO, pursuant to which the Developer must construct and place in-service its proposed project by a set in-service date in a manner consistent with its project proposal.⁸

In performing its evaluation and selection process, the NYISO assesses each proposed transmission project's performance across a broad-range of both cost-based metrics (*e.g.*, capital cost estimates, cost per MW ratio) and non-cost-based metrics (*e.g.*, performance, operability, and expandability of the project). The NYISO evaluates and may select the more efficient or cost effective transmission solution based on the totality of each project's performance across all of the selection metrics. In conducting its evaluation, the NYISO "may engage an independent consultant to review the reasonableness and comprehensiveness of the information submitted by the Developer and may rely on the independent consultant's analysis in evaluating each metric."⁹ While a transmission project's estimated capital cost is an important factor, it is one of many factors evaluated by the NYISO, and project capital cost is not given greater weight than the project's performance across other selection metrics.¹⁰

The Commission accepted the NYISO's selection process for the Public Policy Process as compliant with Order No. 1000.¹¹ In doing so, the Commission rejected arguments from Developers that the NYISO should be required to include specific cost containment metrics

⁶ OATT Section 31.4.2.1 states that "[t]he NYPSC will review all proposed transmission need(s) and, with input from the ISO and interested parties, identify the transmission needs, if any, for which specific transmission solutions should be requested and evaluated."

⁷ A Public Policy Requirement is "[a] federal or New York State statute or regulation, including a NYPSC order adopting a rule or regulation subject to and in accordance with the State Administrative Procedure Act, any successor statute, or any duly enacted law or regulation passed by a local government entity in New York State, that may relate to transmission planning on the BPTFs."

⁸ The *pro forma* Development Agreement is located in Appendix D (Section 31.7) of Attachment Y of the OATT.

⁹ OATT Section 31.4.8.

¹⁰ The Commission rejected the request to make project cost the primary factor in the NYISO's evaluation of proposed transmission solutions. *See, e.g., New York Independent System Operator, Inc., Order on Rehearing and Compliance*, 151 FERC ¶ 61,040 at P 116 (2015); *New York Independent System Operator, Inc., Order on Rehearing and Compliance*, 148 FERC ¶ 61,044 at PP 251-251 (2014).

¹¹ *See, e.g., New York Independent System Operator, Inc., Docket Nos. ER13-102-12, et al., Order Conditionally Accepting Tariff Revisions and Requiring Further Compliance*, 153 FERC ¶ 61,342 (December 23, 2015); *New York Independent System Operator, Inc., Order Conditionally Accepting Tariff Revisions and Requiring Further Compliance*, 162 FERC ¶ 61.107 (February 15, 2018); *New York Independent System Operator, Inc., Letter Order*, Docket Nos. ER13-102-012, -013, -014 (June 5, 2018) (accepting NYISO's March 19, 2019 compliance filing).

among its selection criteria. The Commission indicated that the NYISO's evaluation criteria "are broad enough to allow NYISO to appropriately assess the cost-effectiveness of proposed transmission solutions" and referenced the NYISO's ability to consider in its selection process the accuracy of proposed cost estimates and potential issues associated with delay in constructing the solution.¹² These criteria have enabled the NYISO to evaluate the overall capital costs of transmission solutions in selecting among transmission projects.¹³

The NYISO's current tariffs do not provide Developers the ability to voluntarily submit cost containment proposals and do not include specific metrics by which the NYISO can evaluate cost containment commitments in ranking and selecting transmission projects. Moreover, the tariffs contain no provisions for the NYISO to enforce cost containment commitments made by Developers. Instead, the tariffs state that "[a]ctual project cost recovery, including any issues related to cost recovery and project cost overruns, will be submitted to and decided by the Commission."¹⁴

Although project cost is an important consideration in determining the relative efficiency and cost-effectiveness of competing proposals,¹⁵ the Commission has not required that Independent System Operators ("ISOs") and Regional Transmission Organizations ("RTOs") provide specific metrics to evaluate and select transmission projects based upon Developers' cost containment measures.¹⁶ The Commission held a technical conference on transmission project cost containment and other issues related to competitive transmission development in 2016, in which the NYISO participated.¹⁷ To date, the Commission has not issued further generic guidance on cost containment. The Commission has, however, noted that cost containment

¹² *New York Independent System Operator, Inc.*, 151 FERC ¶ 61,040, at P 117 (2015).

¹³ The NYISO has indicated to stakeholders and Developers that if it were to receive two projects that were completely equally ranked under the NYISO's selection metrics, the NYISO could consider a proposed cost containment mechanism in one of the projects as a tiebreaker in its selection of the more efficient or cost effective project. This is based on the NYISO's ability to review the accuracy of Developer's proposed capital costs estimates. See OATT Section 31.4.8.1.1. These circumstances are unlikely to arise and have not arisen in the NYISO's selection process to address the Public Policy Transmission Needs that have been identified to date.

¹⁴ OATT Section 31.4.8.2 (revised in filing to Section 31.4.8.3).

¹⁵ The Commission has rejected protests that cost should be treated as the primary factor in the NYISO's evaluation of proposed transmission solutions, indicating instead that "Order No. 1000 requires NYISO to consider the relative efficiency and cost-effectiveness of proposed transmission solutions." *New York Independent System Operator, Inc.*, Order on Rehearing and Compliance, 151 FERC ¶ 61,040 at P 116 (2015).

¹⁶ See, e.g., *New York Independent System Operator, Inc.*, Order on Rehearing and Compliance, 151 FERC ¶ 61,040 at P 117 (2015); *New York Independent System Operator, Inc.*, Order on Rehearing and Compliance, 148 FERC ¶ 61,044 at P 251 (2014); see also *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, Order No. 1000 at P 704, FERC Stats. & Regs. ¶ 31,323 (2011) ("Order No. 1000"), order on reh'g, Order No. 1000-A at P 625, 139 FERC ¶ 61,132 ("Order No. 1000-A"), order on reh'g, Order No. 1000-B, 141 FERC ¶ 61,044 (2012), *aff'd sub nom. S.C. Pub. Serv. Auth. v. FERC*, 762 F.3d 41 (D.C. Cir. 2014).

¹⁷ See *Competitive Transmission Development Rates Technical Conference*, Notice of Technical Conference, Docket No. AD16-18-000 (March 17, 2016); see also *id.*, Response of the New York Independent System Operator to Post-Technical Conference Questions, Docket No. AD16-18-000 (October 3, 2016).

could be considered as part of a region's stakeholder process,¹⁸ and the Commission has accepted the use of such measures in other ISO/RTO regions.¹⁹

As part of the “lessons learned” process that the NYISO conducted with its stakeholders after the completion of its first Public Policy Process in 2016, stakeholders identified the addition of a cost containment mechanism in the Public Policy Process as an important area for further consideration. Along with other process reforms, the NYISO considered different potential approaches to cost containment throughout 2017. The NYISO developed a straw proposal for a proposed cost containment approach, which was discussed and further developed with stakeholders at numerous meetings of the Electric System Planning Working Group (“ESPWG”) and of the Transmission Planning Advisory Subcommittee (“TPAS”) from fall 2018 through summer 2019. The NYISO worked with stakeholders in group meetings and one-on-one discussions to fully understand and balance the interests of, and address the concerns raised by, all stakeholder sectors. As discussed in Part IV below, the proposed tariff amendments implementing cost containment were approved for filing at the Commission by the NYISO's Business Issues Committee, Management Committee, and the Board of Directors.

In a parallel stakeholder process resulting from its lessons learned initiative, the NYISO held stakeholder meetings on the respective rights of Transmission Owners and non-incumbent Developers related to upgrades proposed by non-incumbent Developers to Transmission Owners' existing transmission facilities. As part of those discussions, questions were raised on the application of cost containment if a Transmission Owner elected to build, own and recover the costs of the upgrades to its existing transmission facilities. The NYISO proposed to focus on establishing the framework of cost containment in this Section 205 filing, and to consider the cost containment treatment for such upgrades in future stakeholder discussions.²⁰

IV. DESCRIPTION OF PROPOSED TARIFF REVISIONS

The NYISO proposes to revise Sections 31 (Attachment Y) and 6.10 (Rate Schedule 10) of the OATT to establish provisions for cost containment of transmission projects proposed by Developers in its Public Policy Process. As detailed below, the NYISO's proposed revisions will establish: (A) the cost containment mechanisms that a Developer may voluntarily include as part of a proposed Public Policy Transmission Project in the Public Policy Process; (B) how the NYISO will evaluate in a quantitative and qualitative manner cost containment commitments made by Developers to select the more efficient or cost effective transmission solution to a Public Policy Transmission Need; (C) the manner in which cost containment commitments will be implemented as part of the rate recovery for a selected transmission project; (D) the requirements to include any cost containment commitment in the *pro forma* Development Agreement that must be entered into between the NYISO and the Developer of the selected project; and (E) additional, related tariff revisions.

¹⁸ Order No. 1000-A at P 625.

¹⁹ See, e.g., California Independent System Operator Corp. Tariff, Sections 24.5.1, 24.5.2.3, 24.6, Appx. X Section 10.1.1; Midcontinent Independent System Operator, Inc. Tariff, Att. FF Sections VIII.D.5.5, VIII.D.5.6, VIII.E.1.1, Appx. 1 Sections 9.2.

²⁰ See OATT Section 31.6.4.

A. Cost Containment Mechanism

The NYISO proposes to establish tariff mechanisms by which a Developer may voluntarily include a binding cost containment commitment – a “Cost Cap”²¹ – as part of its proposed transmission solution in the Public Policy Process.²² A Developer is not required to propose a Cost Cap for the consideration of its transmission project in the Public Policy Process. However, if it elects to do so the Developer must satisfy the Cost Cap requirements set forth in the OATT, as described below. A Developer that elects to provide a Cost Cap must include it in the project information that it submits to the NYISO in response to the NYISO’s solicitation for proposed solutions.²³

A Cost Cap constitutes a Developer’s binding commitment to contain certain categories of capital costs specified in the OATT – defined as “Included Capital Costs” – in the form of either a hard or a soft cap.²⁴ All other categories of capital costs – “Excluded Capital Costs” – will not be subject to the Cost Cap.²⁵ With the exception of the Cost Cap, all other issues associated with a Developer’s cost recovery for its selected transmission project (*e.g.*, return on equity, prudence of recoverable costs) will be determined by the Commission.²⁶ The NYISO proposes to establish the following requirements concerning the Included Capital Costs, Excluded Capital Costs, and the permissible forms of the Cost Cap.²⁷

i. Included Capital Costs

Proposed OATT Section 31.4.5.1.8.1 establishes that a Developer that elects to provide a Cost Cap must propose to contain all of the capital costs that are designated as Included Capital Costs in the OATT.²⁸ The provision defines Included Capital Costs as “all capital costs incurred by a Developer to plan for and construct a Public Policy Transmission Project, and to make it ready for its intended use” with the exception of the Excluded Capital Costs described below.²⁹ The NYISO derived this language from the Generally Accepted Accounting Principles,³⁰ upon which FERC’s Uniform System of Accounts is based.³¹

²¹ The NYISO proposes to insert in the OATT a definition of “Cost Cap,” which shall mean “A Developer’s commitment to contain the capital costs of its proposed Public Policy Transmission Project in accordance with the requirements in Section 31.4.5.1.8. The Cost Cap must be in the form of a hard Cost Cap or a soft Cost Cap as described in Section 31.4.5.1.8.3.” Proposed revision to OATT Section 31.1.1.

²² Proposed OATT Sections 31.4.5.1.1, 31.4.5.1.8.

²³ *Id.*

²⁴ Proposed OATT Sections 31.4.5.1.8, 31.4.5.1.8.1, 31.4.5.1.8.3.

²⁵ Proposed OATT Sections 31.4.5.1.8, 31.4.5.1.8.2.

²⁶ Proposed revisions to OATT Section 31.4.8.3 (previously Section 31.4.8.2), proposed Section 6.10.6.5.

²⁷ See proposed OATT Sections 31.4.5.1.8 to 31.4.5.1.8.4.

²⁸ Proposed OATT Section 31.4.5.1.8.1.

²⁹ *Id.*

³⁰ See Financial Accounting Standards Board, Accounting Standards Codification 360-10-30-1 (Property, Plant, and Equipment – Overall – Initial Measurement – Historical Cost Including Interest).

³¹ See 18 C.F.R. Part 101, Electric Plant Instructions (2018). For purposes of clarity, the enumerated categories of Included Capital Costs in Section 31.4.5.1.8.1 are identical to the corresponding categories set forth in the Electric Plant Instructions in the Uniform System of Accounts in Part 101 of the Commission’s regulations, with the exception of those categories that are considered Excluded Capital Costs.

The proposed tariff provision specifies the categories of capital costs that a Developer must include as Included Capital Cost in the Cost Cap: contract work, labor, materials and supplies, transportation, special machine services, shop services, protection, injuries and damages, privileges and permits, engineering services, the cost of conducting an environmental site assessment or investigation,³² as well as reasonably foreseeable environmental site remediation and environmental mitigation costs (as further described in Part IV(A)(iii) below), general administration services, legal services, real estate and land rights, rents, studies, training, asset retirement, and taxes.³³

The NYISO proposes to provide Developers with flexibility on one particular type of capital cost to either reflect it as an Included Capital Cost (and therefore subject to the Cost Cap) or reflect it as an Excluded Capital Cost (and therefore not subject to the Cost Cap). Specifically, a Developer may choose to reflect as Included Capital Costs real estate costs for existing rights-of-way that are part of the proposed Public Policy Transmission Project, but are not owned by the Developer, such as existing utility rights-of-way.³⁴ For Developers that provide a Cost Cap but choose not to include such costs, the NYISO will employ its independent consultant to estimate the costs of rights-of-way owned by third parties, which is its current approach for valuing rights-of-way for proposed transmission projects.

ii. Excluded Capital Costs

Proposed OATT Section 31.4.5.1.8.2 provides that a Developer may not include costs from the Excluded Capital Costs categories in its Cost Cap.³⁵ The Excluded Capital Costs are capital costs associated with one of the following four categories:

1. Capital costs of system upgrades determined by the NYISO in one of its interconnection processes. These costs will not be known by a Developer during the 60-day transmission project solicitation window in the Public Policy Process. A Developer is only required to have demonstrated that it has submitted a Transmission Interconnection Application for its project at the point in which it submits its project information at the conclusion of the 60-day solicitation window.³⁶ The NYISO will include an independent estimate of interconnection costs in its calculation of total project capital costs to the extent they are known at the time of transmission project evaluation and selection.
2. Debt costs, allowance for funds used during construction (“AFUDC”), and other representations of the cost of financing the transmission project during the construction timeframe that may be included as part of the capital cost of the project when it enters into service or as otherwise determined by the Commission.

³² Proposed OATT Section 31.4.5.1.8.2.1.

³³ Proposed OATT Section 31.4.5.1.8.1.

³⁴ *Id.*

³⁵ Proposed OATT Sections 31.4.5.1.8, 31.4.5.1.8.2.

³⁶ OATT Section 31.4.4.3.4.

Developers may not know these costs during the sixty-day project proposal window. As described above in Part IV(A), the NYISO proposes not to estimate or evaluate a Developer's return on equity, financing costs, or incentives such as construction work in progress ("CWIP") payments.

- 3 Unforeseeable environmental remediation and environmental mitigation costs, as described in Part (IV)(A)(iii) below; and
4. Real estate costs for existing rights-of-way that are part of the proposed Public Policy Transmission Project but are not owned by the Developer if, as described in Part IV(A)(i) above, the Developer elects not to include them as Included Capital Costs. The NYISO will employ its independent consultant to estimate the costs of rights-of-way owned by third parties.³⁷

These Excluded Capital Costs are types of costs that cannot reasonably be estimated or foreseen by Developers within the sixty-day project proposal window with sufficient certainty to subject the costs to the Cost Cap. The Commission has accepted the exclusion of similar categories of costs from cost containment measures in other ISO/RTO areas.³⁸ Accordingly, the NYISO submits that the Commission should accept these provisions as just and reasonable.

iii. Treatment of Environmental Mitigation and Remediation Costs

In general, proposed OATT Section 31.4.5.1.8.1 treats the cost of a Developer's conducting transmission project site investigation and remediation as a capital cost of getting a transmission project ready to enter into service.³⁹ Proposed OATT Section 31.4.5.1.8.1.1(i)-(iii) requires Developers always to include as Included Capital Costs the costs of conducting an environmental assessment of the transmission site, and to also include environmental investigation and remediation costs based upon the extent of their knowledge of such issues as they arise in the normal course of planning and constructing a Public Policy Transmission Project.⁴⁰ Specifically, these sections require the following:

- (i) For project sites for which an environmental site assessment has already been conducted or environmental remediation or mitigation activities are ongoing, the Developer shall provide an estimate of any additional environmental site

³⁷ Proposed OATT Section 31.4.5.1.8.2.

³⁸ See, e.g., MISO Tariff, Attachment FF, Appendix 1 (Selected Developer Agreement), Section 9.2.1 (detailing approved deviations from the proposed cost containment measures, including material changes in the scope of work, unforeseen requirements imposed by Interconnecting Transmission Owner, and increases in project cost expressly authorized by the agreed-upon cost containment measure); see also *PJM Interconnection L.L.C.*, 154 FERC ¶ 61,054 (2016) (accepting Designated Entity Agreement in PJM in Docket No. ER16-429-000 with non-conforming addition in Schedule E of cost containment measure that excludes certain costs from the measure including taxes, financing costs (including AFUDC), costs due to PJM-directed changes in scope of work, costs resulting from Uncontrollable Force, and costs associated with operation and maintenance of project).

³⁹ See 18 C.F.R. Part 101, Electric Plant Instructions (2018).

⁴⁰ Proposed OATT Sections 31.4.5.1.8.1, 31.4.5.8.1.1.

investigation, remediation, or mitigation that is known or reasonably anticipated at the time of submission.

- (ii) For project sites for which the Developer has no reason to believe any environmental remediation or mitigation is required without undertaking a site investigation such as, but not limited to, any greenfield or undeveloped land, the Developer shall provide an estimate of the cost to perform a Phase I Environmental Site Assessment on a per mile basis.
- (iii) For project sites for which the Developer has reason to believe environmental site investigation, remediation, or mitigation may be required, the Developer shall provide an estimate of the cost to perform such environmental site investigation, remediation, or mitigation to the extent possible based upon the information reasonably available to the Developer at the time of submission.⁴¹

The proposed tariff revisions recognize that the precise costs of environmental remediation and mitigation costs are not reasonably foreseeable, especially in the sixty-day project proposal window. Accordingly, proposed OATT Section 31.4.5.1.8.2.1 defines as Excluded Capital Costs “unforeseeable environmental remediation and environmental mitigation costs,” described as:

any costs relating to environmental remediation and environmental mitigation that are not anticipated by the Developer or are otherwise indeterminable based upon information reasonably available to the Developer at the time of submission, including any environmental remediation or mitigation costs that cannot be estimated by the Developer without performing an environmental site assessment or investigation Costs attributable to environmental investigation, remediation, and mitigation that exceed the amount estimated in the Developer’s bid based on, among other things, changes in the extent of known contamination will be considered “unforeseeable environmental remediation and environmental mitigation costs” and Excluded Capital Costs.⁴²

In sum, Developers that voluntarily submit a Cost Cap are expected to include their known site investigation and remediation costs. For Developers that do not submit a voluntary cost containment proposal, the NYISO will employ its independent consultant to calculate cost estimates of known environmental investigation and remediation costs to include in the projects’ capital cost estimates. The NYISO will not estimate or include unforeseeable environmental remediation and mitigation costs in calculating transmission projects’ total capital costs. The NYISO developed these classifications of environmental remediation and mitigation costs with Transmission Owners, other Developers, and its independent consultants, and submits that they represent a just and reasonable treatment of such costs for Cost Caps.

⁴¹ Proposed OATT Section 31.4.5.1.8.1.1(i)-(iii).

⁴² Proposed OATT Section 31.4.5.1.8.2.1.

iv. Forms of Cost Cap

Proposed OATT Section 31.4.5.1.8 provides that a Developer may submit a Cost Cap either in the form of a hard Cost Cap or a soft Cost Cap.⁴³ Proposed OATT Section 31.4.5.1.8.3 defines a hard Cost Cap for Included Capital Costs as “a dollar amount for those costs above which the Developer commits in its proposed Public Policy Transmission Project not to recover from ratepayers.” That is, if a Developer proposes a hard Cost Cap for its Included Capital Costs, the Developer will not be eligible to recover from ratepayers its actual costs for the Included Capital Costs that exceed the capped amount. The provision also defines a soft Cost Cap for Included Capital Costs as “a dollar amount for those costs above which the Included Capital Costs are shared between the Developer and ratepayers based on a defined percentage.”⁴⁴ The NYISO will assess a transmission project’s estimated costs and the benefits of the Cost Cap differently based on whether the Developer proposed a hard Cost Cap or a soft Cost Cap.

Proposed OATT Section 31.4.5.8.3 states that if a Developer elects to propose a soft Cost Cap for its Included Capital Costs, the Developer’s percentage of cost sharing under a soft Cost Cap shall be at least twenty (20) percent (“20%”).⁴⁵ As described in the accompanying Affidavit of Lorenzo Seirup, Supervisor of Market Mitigation and Analysis, the NYISO adopted this minimum 20% for a Developer’s share of cost overruns because values less than that sharing level are unlikely to provide any incentive to Developers to actually contain their capital costs. When a Developer’s share of cost overruns is 20% or greater, the Developer’s profit motive aligns with ratepayers’ interests in avoiding cost overruns.⁴⁶ This “alignment” between the Developer’s profit motive and the minimization of cost overruns (which can be thought of as the consumer’s “profit motive”) occurs when incremental costs in excess of the agreed-upon Cost Cap are accompanied by a financial loss on the part of the Developer, and thus a decrease in the overall value of the project to the Developer’s shareholders.

To determine the appropriate minimum cost sharing amount, the NYISO calculated the Net Present Value of an incremental cost overrun to a hypothetical Developer under a variety of cost sharing amounts using generic financing and cost of capital assumptions. This analysis showed that, for the hypothetical Developer studied, the “break-even” point, *i.e.*, the point at which the Developer was financially indifferent to an incremental cost overrun was just slightly above 20%. As cost-sharing levels rose above 20%, the Developer had an increasingly strong profit motive to avoid cost-overruns. Below 20%, the Developer earned additional profit with a cost overrun, even though it forwent recovery of a portion of that overrun.

The NYISO’s proposed limitation on soft Cost Caps enhances the application of the proposed quantitative and qualitative metrics described in Part IV(B) below. It does so by “shifting the starting line” at which the effectiveness of each cost containment proposal is

⁴³ Proposed OATT Section 31.4.5.1.8.3.

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ Affidavit of Lorenzo Seirup (December 13, 2019) (“Seirup Affidavit”), at PP 7-21.

measured to a point that better represents the “conceptual zero”⁴⁷ of effectiveness in incenting Developers to avoid cost overruns. In addition, the proposed limitation on soft Cost Caps provides for greater confidence in “apples-to-apples” comparisons between transmission solutions by precluding cost containment proposals with cost sharing amounts that are likely to be ineffective. For these reasons, which are supported by the Affidavit of Lorenzo Seirup, the NYISO submits that the Commission should accept as just and reasonable the 20% floor on Developers’ share of cost overruns in a soft Cost Cap.⁴⁸

B. NYISO’s Assessment of Cost Caps in Its Evaluation and Selection Process

The NYISO proposes to revise the selection metrics of its Public Policy Process to establish the manner in which it will assess Cost Caps proposed by Developers as one consideration among a host of metrics that the NYISO utilizes to evaluate and select the more efficient or cost effective transmission solution to a need.⁴⁹ The current evaluation metrics accepted by FERC employ both quantitative and qualitative approaches to evaluating and ranking transmission projects. Consistent with that approach, the NYISO’s proposed metrics evaluate Developers’ capital cost containment commitments quantitatively and qualitatively. These revisions enhance the NYISO’s approach of evaluating each project based on the totality of its performance across the broad-range of all cost and non-cost based selection metrics.

In these tariff amendments, the NYISO is proposing a standardized process to address certain categories of capital costs across all transmission projects. The NYISO submits that limiting its proposal to capital costs is just and reasonable for several reasons. First, transmission project capital costs constitute the largest category of costs that will be recovered through rates approved by the Commission. Therefore, cost containment concerning capital cost recovery provides meaningful protection to ratepayers against cost overruns. Second, a Developer’s competitiveness on capital costs is also a reasonable indicator of its competitiveness on project costs overall. Finally, the NYISO’s current Commission-approved process is limited to consideration of capital costs. The NYISO has retained independent consultants to evaluate project capital costs, contingencies, and escalation factors, and has successfully utilized those experts in three competitive selections in its Public Policy Process.

Certain ISO/RTOs, such as the Midcontinent Independent System Operator and the Southwest Power Pool, permit Developers to propose cost containment mechanisms that are different from a standard cost cap.⁵⁰ As a result, Developers propose a wide variety of rate mechanisms to address cost overruns and/or project-specific categories of costs to be included in and excluded from proposed caps. The NYISO reviewed these ISO/RTOs’ processes and

⁴⁷ The “conceptual zero” is the point at which a Developer is financially indifferent to an incremental cost overrun. That is, cost-sharing amounts above this point provide a financial incentive for the Developer to minimize cost overruns, while cost sharing amounts below this point do not, or may even have the opposite effect. Seirup Affidavit P 18 fn. 9.

⁴⁸ Seirup Affidavit at PP 7-18.

⁴⁹ Proposed OATT Section 31.4.8.2.

⁵⁰ See *Midwest Independent Transmission System Operator, Inc.*, 147 FERC ¶ 61,127 at P 363 (2014); *Southwest Power Pool*, 144 FERC ¶ 61, 059 at P 308 (2013).

identified a number of challenges that would be associated with implementing them in New York.

Based on ongoing efforts to streamline its planning processes, the NYISO seeks to avoid extending the time required to complete its evaluation and selection process. To conduct a process that requires the NYISO to assess multiple and widely varying types of cost containment mechanisms would engage the NYISO in a lengthy evaluation process that could add months to its evaluation of the more efficient or cost effective project. By comparison, the NYISO's proposal provides for standardized, "apples to apples" comparisons of proposals that cap the same categories of capital costs, with limited variations on the cap types that are prescribed in the tariffs.

Adopting a cost containment mechanism that allows Developers to choose from among all categories of costs would require the NYISO to expend significant additional resources and time to procure expertise and evaluate rate matters such as capital structure, financing costs, return on equity, treatment of debt costs, AFUDC and CWIP payments, return on equity, other rate incentives, and short-run and long-run operation and maintenance costs of transmission projects over the decades-long useful life of the asset. These matters are often subject to extensive rate proceedings and settlement conferences at the Commission, and analyzing them in the planning process would introduce the prospect of months of additional analysis. An open-ended approach to all cost categories would also require the NYISO to attempt to predict the outcome of Commission rate proceedings on individual project or formula rates. Alternatively, requiring that a Developer seek pre-approval or a rate determination by the Commission concerning its cost containment proposal prior to the NYISO's selection would erect a hurdle to project proposals, lead to numerous additional proceedings at the Commission, and significantly extend the time to complete the Public Policy Process.

In sum, the NYISO will fairly and evenly apply the proposed cost containment mechanism to multiple project proposals from many Developers without adding significant time to its current evaluation and selection process. Accordingly, the NYISO respectfully submits that the Commission should accept its proposal, as detailed below, as just and reasonable.

i. Quantitative Evaluation

Section 31.4.8.1 of the OATT establishes the selection metrics that the NYISO uses in its evaluation and selection of proposed transmission projects in the Public Policy Process. A number of the selection metrics evaluate or are impacted by the proposed project's estimated cost. These include the capital costs estimates for the project, including the accuracy of the proposed estimate; the costs per MW ratio of the proposed project; additional metrics that may be proposed by the NYPSC; and other metrics that the NYISO may consider in consultation with its stakeholders (*e.g.*, changes in production costs).⁵¹

⁵¹ OATT Sections 31.4.8.1.1, 31.4.8.1.3 (revised from 31.4.8.1.2), 31.4.8.1.9 (revised from 31.4.8.1.8), and 31.4.8.1.10 (revised from 31.4.8.1.9).

The NYISO currently engages independent consultants to review the project information submitted by a Developer, including its project cost estimate, and relies on the independent consultants' analyses and estimates in evaluating projects' performance under each metric.⁵² The NYISO proposes to establish a new Section 31.4.8.2.1 of the OATT to estimate the total capital costs of each proposed transmission project that the NYISO will use for purposes of assessing the performance of a proposed transmission project under the cost-based metrics.

In the selection process, the NYISO will calculate the total capital costs for each proposed transmission project by adding the amount of the Included Capital Costs for the project to that of Excluded Capital Costs. The NYISO will use the amount of Included Capital Costs from Developers that provide a Cost Cap, and will use its independent consultants' estimates for Included Capital Cost items for Developers that do not provide a Cost Cap. The NYISO will use its independent consultant to estimate the amounts of Excluded Capital Costs in all instances. Certain capital costs that are unforeseeable, such as costs related to unforeseeable environmental remediation or mitigation costs, will not be added into the calculation of projects' total capital costs. The NYISO will determine the amounts for Included Capital Costs and Excluded Capital Costs that comprise total capital costs in the following manner.⁵³

a. Included Capital Costs

The amount for Included Capital Costs that the NYISO will use in the calculation of the total capital cost for the selection process will depend upon whether the Developer has elected to use a Cost Cap and which form of Cost Cap it has proposed.

If a Developer does not elect to submit a Cost Cap, the NYISO will continue to rely on its independent consultant to estimate the Included Capital Cost amount.⁵⁴ If a Developer elects to submit a hard Cost Cap, the NYISO will use the amount of the hard Cost Cap submitted by the Developer as the amount for the Included Capital Costs.⁵⁵ The NYISO will use the capped amount because the Developer has agreed to be bound to that amount.

If a Developer elects to submit a soft Cost Cap and the capped amount is above the amount estimated by the NYISO's independent consultant, the NYISO proposes to use the amount of the soft Cost Cap as the amount for the Included Capital Costs.⁵⁶ In such case, it is reasonable to use the Developer's own cost estimate for several reasons. First, allowing a Developer that bids above the independent estimate to benefit from the lower independent estimate in project evaluation provides the wrong incentive to Developers. To maximize the benefits of competitive cost containment to ratepayers, Developers should have an incentive to beat the independent cost estimate by bidding below what it expects will be the independent estimate for its project. This expectation is borne out by the NYISO's experience in its three transmission selection processes to date. The majority of Developers' cost estimates in projects

⁵² See OATT Section 31.4.8.

⁵³ Proposed OATT Sections 31.4.8.1.1, 31.4.8.2.1.

⁵⁴ Proposed OATT Section 31.4.8.2.1.

⁵⁵ Proposed OATT Section 31.4.8.2.1.1.

⁵⁶ Proposed OATT Section 31.4.8.2.1.2.

proposed to meet the Western New York need, and all of the Developers' cost estimates in projects proposed to meet Segment A and Segment B of the AC Transmission needs were below the NYISO's independent cost estimate. In the event that a Developer does bid above the independent estimate, it is either because there is an aspect of its project that is unusual and the Developer knows best what its costs will be, or because the Developer elects not to accept much cost risk with its project. Accordingly, the NYISO submits that it is just and reasonable to evaluate a Developer's project at its bid cost for Included Capital Costs if its bid cost exceeds the independent consultant's cost estimate.

If, however, a Developer elects to submit a soft Cost Cap and the capped amount is below the amount estimated by the NYISO's independent consultant, the NYISO will calculate an adjusted value for the Included Capital Costs.⁵⁷ As a soft Cost Cap exposes ratepayers to some percentage of costs in excess of the Cost Cap, the NYISO proposes not to simply use the proposed Cost Cap as the anticipated value of Included Capital Costs. Instead, the NYISO will calculate an adjusted value of the Included Capital Cost that is based upon the level of ratepayer exposure to cost overruns. Specifically, the NYISO will (i) multiply the difference between (a) the independent consultant's cost estimate for Included Capital Costs and (b) the Developer's Included Capital Costs, by (c) the risk percentage assumed by ratepayers; and (ii) add that amount to the Developer's Included Capital Costs.⁵⁸ An example illustrating the application of this adjusted value is provided in Part IV(B)(iii) below. The NYISO submits that this approach is just and reasonable because it appropriately reflects the level of ratepayer exposure to cost overruns within this metric.

b. Excluded Capital Costs

Proposed OATT Section 31.4.8.2.1 provides that the NYISO's independent consultant will estimate the costs of Excluded Capital Costs.⁵⁹ However, for the reasons discussed above in Part IV(B)(i), the NYISO will not estimate and will not include in its calculation of the total capital costs of proposed transmission projects certain categories of Excluded Capital Costs that are not foreseeable or that involve rate matters that would extend the evaluation time period. These are: (i) any costs concerning unforeseeable environmental mitigation or remediation costs, and (ii) any costs concerning the financing of the proposed transmission project, including debt costs, AFUDC, and any other financing costs.⁶⁰

c. Contingency/Escalation

Proposed OATT Section 31.4.5.1.8.4 requires a Developer to specify any contingency percentage and escalation factors applicable to the Included Capital Costs in its Cost Cap. If a Developer does not address contingency and escalation in its Cost Cap, the NYISO will not add those elements when it evaluates the project's total capital costs. For any portions of the total capital costs of a Public Policy Transmission Project where the estimate from the independent

⁵⁷ *Id.*

⁵⁸ *Id.*

⁵⁹ Proposed OATT Section 31.4.8.2.1.

⁶⁰ *Id.*

consultant is used (rather than a proposed Cost Cap), the ISO and its independent consultant may add appropriate contingency percentages and escalation factors.⁶¹ This approach is reasonable because the NYISO currently uses its independent consultant to apply contingency and escalation factors to proposed transmission projects. Proposed OATT Section 31.4.4.3.1 provides that before issuing a solicitation for solutions, and to the extent practicable, the NYISO will present to Developers and interested parties any contingency percentage and escalation factors that its independent consultant will use.⁶²

ii. Qualitative Evaluation

The NYISO proposes to insert a new selection metric as Section 31.4.8.1.2 concerning the NYISO's qualitative evaluation of any Cost Cap that was voluntarily submitted by a Developer. In addition, the NYISO proposes to establish a new Section 31.4.8.2.2 to detail how the NYISO will assess proposed transmission projects under the new qualitative metric.

The quantitative evaluation of a project's costs may make a proposed project appear favorable compared to competitors, which project, nevertheless, has an increased risks of cost overruns. Conversely, a project may have a relatively higher capital Cost Cap compared to competing projects, but may carry a comparatively lower risk of cost overruns. These scenarios demonstrate that a purely quantitative evaluation of capital Cost Caps alone does not provide a comprehensive evaluation of the quality of capital cost containment commitments. Accordingly, the NYISO proposes to evaluate the quality of capital Cost Caps considering the following risk factors:

- The effectiveness of the proposed Cost Cap in providing an incentive to the Developers to contain their Included Capital Costs, *i.e.*, how aligned is the Developer's incentive to maximize its profits by avoiding cost overruns compared to the level of risk exposure to consumers, and what degree of risk is the Developer assuming to pay for cost overruns;
- The effectiveness of the proposed Cost Cap in protecting ratepayers from Included Capital Cost overruns; and
- The magnitude of the difference between the Cost Cap and the independent cost estimate. If the cost-contained estimate provided by a Developer is significantly below the NYISO's independent cost estimate, the NYISO will consider the likelihood that the project will be constructed at the capped cost, given the Developer's financial and technical qualifications. Conversely, if the Developer's cost-contained estimate is significantly above the independent cost estimate, the NYISO will consider whether the proposed Cost Cap will meaningfully contain capital costs.⁶³

These factors will allow the NYISO to assess project cost overrun risk factors that are not easily quantified. For example, the NYISO can easily calculate the dollar level of ratepayer risk

⁶¹ Proposed revisions to OATT Section 31.4.8.

⁶² Proposed revisions to OATT Section 31.4.4.3.1.

⁶³ Proposed OATT Section 31.4.8.2.2.

exposure to cost overruns in Hard Cap and Soft Cap proposals. Nevertheless, dollar values alone do not address how effective the proposal is in reducing the likelihood and magnitude of cost overruns, and in diminishing the financial exposure of ratepayers to cost overruns that do occur.

If the Cost Cap proposed by the Developer is much lower than the cost estimates assessed by the NYISO's independent consultants, the proposed tariff authorizes the NYISO to request additional technical and financial capability information from the Developer to better assess the risk of under-estimation to project completion.⁶⁴ If the NYISO determines that the Developer's cost containment commitment is unrealistically low, the cost containment commitment will receive a relatively lower ranking because of the low probability that the Developer could complete the project at the Cost Cap amount. If the Cost Cap proposed by the Developer is much higher than the cost estimates assessed by the independent consultants, the Cost Cap will likely not be meaningful in protecting ratepayers from cost overruns because it may not have any binding effect on the Developer. Such a cost containment mechanism will receive a relatively lower qualitative ranking than a cost containment proposal that is more likely to contain project costs.

iii. Example

The following example illustrates how the NYISO will estimate the total capital cost amount for use in the cost-based selection metrics (*e.g.*, cost estimates, cost per MW, and benefit-cost ratios) based on the cost containment mechanism proposed by a Developer and the amount of risk assumed by the Developer, as well as how the qualitative evaluation will be carried out. For purposes of this example, assume that a transmission proposal was submitted by Developer A without a cost containment commitment. In addition, three transmission proposals were submitted to the NYISO by Developers B, C, and D. All three proposals provide a Cost Cap of \$300 million, but with three different risk sharing structures. Developer B proposes a soft Cost Cap of 80/20 risk sharing (80% to ratepayers, 20% to Developer); Developer C proposes a soft Cost Cap of 50/50 risk sharing; and Developer D proposes a hard Cost Cap of 0/100 risk sharing. The appropriate contingency percentage and escalation factors are already calculated in these cost estimates.

⁶⁴ *Id.*

Illustrative Example: Comparison of Cost Containment Mechanism

		Developer A		Developer B		Developer C		Developer D	
		No cost containment proposal		80/20 Risk Share		50/50 Risk Share		0/100 Risk Share	
	Note	Contained Costs	Excluded Costs	Contained Costs	Excluded Costs	Contained Costs	Excluded Costs	Contained Costs	Excluded Costs
Developer Proposal	a	300	N/A	300	N/A	300	N/A	300	N/A
Independent Estimate	b	400	75	400	75	400	75	400	75
Overrun Risk	c = b - a	N/A		100	N/A	100	N/A	N/A	N/A
Ratepayer's Share of Overrun	d = c*risk sharing	N/A	75	80	75	50	0	0	75
Adjusted Estimate	e = a + d	400	75	380	75	350	300	300	75
Total Capital Costs for Quantitative Evaluation	Total Costs	475		455		425		375	

From a quantitative perspective, although the cost estimates initially proposed by the Developers in this example are the same, the total capital costs that the NYISO will use in assessing the projects under its cost-based selection metrics will differ based on the risk sharing percentage assumed by the Developer. The higher amount of risk directed at ratepayers, the higher the total capital costs estimate.

Qualitatively speaking, Developer D with a hard cap is best motivated to contain the cost so it will not encounter any losses due to cost overruns. As a result, the Developer's profit motive to minimize cost overruns is best aligned with the hard cap (0/100 risk sharing), as well as the minimum risk to ratepayers to pay for the cost overruns. Accordingly, Developer D is ranked the best for this proposed qualitative metric, followed by the 50/50 cost sharing proposal by Developer C, and then the 80/20 cost sharing proposal by Developer B. Developer A will not be evaluated in this metric since it does not provide any cost containment mechanism.

C. Implementation of Cost Cap for Developer's Cost Recovery

Rate Schedule 10 of the NYISO's OATT establishes the mechanism by which the Developer of a transmission project selected in the Public Policy Process may recover its project

costs under the OATT. Pursuant to these requirements, the Developer (or the NYISO, at the Developer's request) must file under Section 205 with the Commission or make an informational filing under an existing formula rate to provide for the Commission's review and approval or acceptance of the project costs and the resulting revenue requirement to be recovered under Rate Schedule 10.⁶⁵ The costs eligible for recovery include all reasonably incurred costs, as determined by the Commission, related to the preparation of proposals for, and the development, financing, construction, operation, and maintenance of the transmission project.⁶⁶ These costs also include a reasonable rate of return on investment and any incentives for the construction of transmission projects approved by the Commission.⁶⁷

The NYISO proposes to insert a new Section 6.10.6 in Rate Schedule 10 to establish the manner in which a Developer's Cost Cap will be implemented as part of the Developer's recovery of its project costs.⁶⁸

i. Submission and Implementation of Cost Cap

Proposed amendments to Rate Schedule 10 and Section 31.4 of the OATT will require the Developer of a selected transmission project to file with the Commission any Cost Cap that it proposed as part of the rate for its project.⁶⁹ In addition, the NYISO proposes to amend the *pro forma* Development Agreement between the NYISO and Developer to include the Cost Cap proposed by the Developer of a selected project, which requirements are detailed in Part IV.D below.⁷⁰

The proposed revisions prohibit the Developer from seeking, and require the Developer to agree in the Development Agreement that it will not seek to recover, either through its transmission rates or through any other means, costs it incurs for Included Capital Costs above its agreed-upon Cost Cap.⁷¹ The NYISO will monitor and seek to enforce Cost Caps for Included Capital Costs contained in the Development Agreements it enters into with Developers in rate proceedings at the Commission.⁷²

Finally, Proposed Section 6.10.6.5 provides that all other matters concerning a Developer's recovery of the costs of its transmission project will be submitted and decided by

⁶⁵ OATT Sections 6.10.4.2, 6.10.5.2.2, 6.10.5.3.1.

⁶⁶ OATT Sections 6.10.4.1, 6.10.5.1.

⁶⁷ *Id.*

⁶⁸ The NYISO also proposes revisions to Sections 6.10.4.1, 6.10.4.2, 6.10.5.1, 6.10.5.2.2, and 6.10.5.3.1 to clarify that the existing cost recovery requirements for Developers that proposed a Cost Cap for a Public Policy Transmission Project are subject to this new Section 6.10.6.

⁶⁹ Proposed OATT Sections 6.10.6.1, 31.4.5.1.8, proposed revisions to Sections 31.4.8.3 (revised 31.4.8.2).

⁷⁰ Proposed OATT Sections 6.10.6.4, 31.4.5.1.8; proposed revisions to Sections 31.4.8.3 (revised 31.4.8.2), 31.4.12.2.

⁷¹ Proposed OATT Sections 6.10.6.1, 31.4.5.1.8; proposed revisions to Section 31.4.8.3 (revised 31.4.8.2). This requirement is consistent with the language used in other ISO/RTOs' development agreements concerning a Developer not recovering costs above its agreed-upon cost containment measure. *See* MISO Tariff, Attachment FF, Appendix 1 (Selected Developer Agreement), Section 9.2; CAISO Tariff, Appendix X (Approved Project Sponsor Agreement), Section 10.1.1.

⁷² Proposed OATT Section 6.10.6.4.

the Commission pursuant to the existing requirements in Rate Schedule 10 concerning a Developer's recovery of its costs.⁷³

ii. Excusing Conditions

The NYISO proposes to establish limited, specified excusing conditions from the Cost Cap.⁷⁴ Proposed OATT Section 6.10.6.2 provides that a Developer may recover costs above its agreed-upon Cost Cap for Included Capital Costs only to the extent that such costs arise from the excusing condition.⁷⁵ The excusing conditions are: (i) Transmission Project changes, delays, or additional costs that are due to the actions or omissions of the ISO, Connecting Transmission Owner(s), Interconnecting Transmission Owner(s), or Affected Transmission Owner(s); (ii) a *Force Majeure* event as defined in the Development Agreement and subject to the *Force Majeure* requirements in Article 15.5 of the Development Agreement; (iii) changes in laws or regulations, including but not limited to applicable taxes; (iv) material modifications to scope or routing arising from siting processes under Public Service Law Article VII or applicable local laws as determined by the New York State Public Service Commission or local governments respectively; and (v) actions or inactions of regulatory or governmental entities, and court orders.⁷⁶

The NYISO developed these excusing conditions with input from its stakeholders. They constitute the limited circumstances in which a Developer could not reasonably anticipate increases to the Included Capital Costs contained in its Cost Cap and for which it would be unreasonable not to permit those costs to be recoverable.⁷⁷ The Developer must file the excusing conditions along with the Cost Cap at the Commission, and the excusing conditions must be included along with the Cost Cap in the Development Agreement.⁷⁸ The NYISO submits that the excusing conditions are consistent with those accepted by the Commission for other regions,⁷⁹ and requests that the Commission accept them as just and reasonable.

iii. Alternative Rate Methodology

Proposed Section 6.10.6.3 of Rate Schedule 10 requires a Developer to achieve the percentage cost sharing that it submitted to the NYISO in a soft Cost Cap. The tariff requires the Developer to:

achieve the percentage cost sharing that it submits to the ISO in its proposal either: (i) through foregoing rate recovery of that percentage of capital costs in excess of the soft cost Cost Cap or (ii) through an alternative rate mechanism that may adjust rate

⁷³ Proposed OATT Section 6.10.6.5.

⁷⁴ Proposed OATT Section 6.10.6.2.

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ Notwithstanding the NYISO's determination that certain costs should be eligible for cost recovery, a Developer must still demonstrate to the Commission that such costs were reasonably incurred.

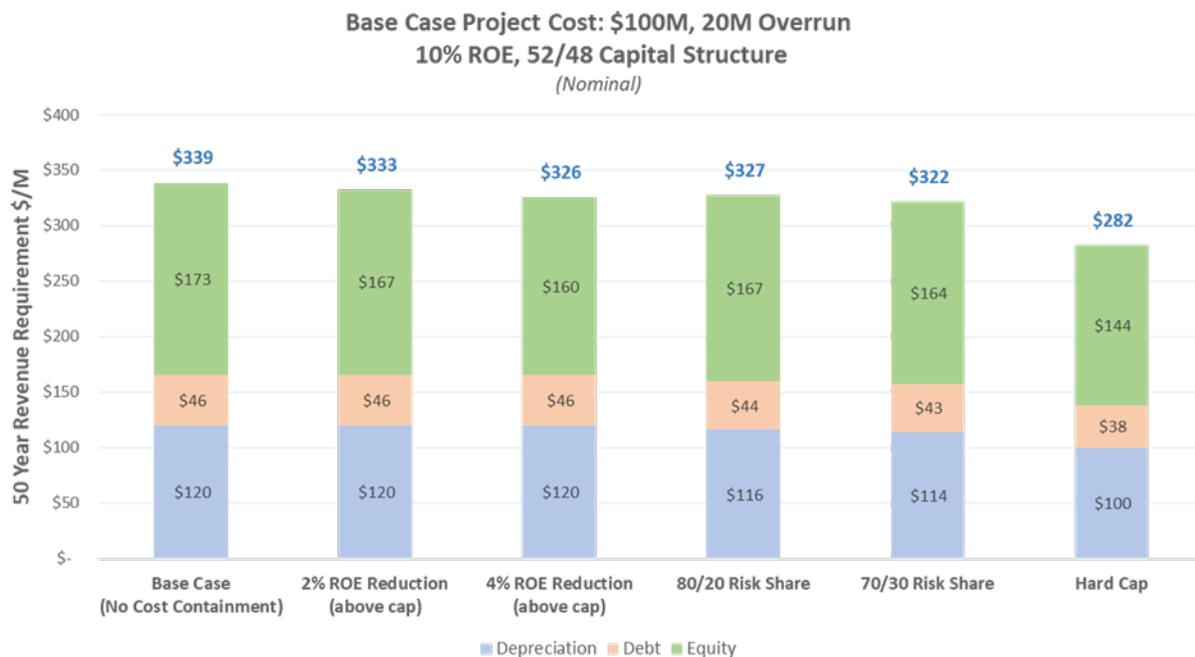
⁷⁸ Proposed OATT Sections 6.10.6.1, 6.10.6.2, 6.10.6.4.

⁷⁹ See footnote 38 above.

recovery through only a reduction in the return on equity and any applicable incentives solely on the amount in excess of the soft Cost Cap.⁸⁰

In considering this approach, the NYISO evaluated hypothetical cost recovery reductions achieved through lower returns on equity applied to amounts in excess of a cap. Based upon its analysis, the NYISO determined that Developers could potentially absorb the Developer’s share of the capital cost overrun through a lower return on equity on the capital cost overrun amount over the useful life of the asset. That is, the NYISO determined that in some circumstances the total long-term revenue reduction for a transmission project could be achieved either through directly foregoing recovery of the Developer’s share of the overrun amounts, or through a lower rate of return applied to the overrun amounts.⁸¹ Implementation is not always possible, however, and it must therefore be verified on a case-by-case basis.

The following example illustrates the NYISO’s analysis. For purposes of this example, the NYISO compares different revenue requirements for a hypothetical project that has \$100 million project cost, \$20 million cost overrun, 10% return on equity, and 52/48 capital structure. The example demonstrates that, in this scenario, a 4% return on equity reduction would achieve a long-term revenue reduction that is slightly greater than the long-term revenue reduction achieved using a 80/20 risk share.



Accordingly, the NYISO proposes that it would be just and reasonable to permit a Developer that has submitted a soft Cost Cap to achieve the percentage cost sharing it submitted

⁸⁰ Proposed OATT Section 6.10.6.3.

⁸¹ Seirup Affidavit at PP 19-21.

in its proposal in one of two ways.⁸² The Developer may forego rate recovery of that percentage of capital costs in excess of the soft Cost Cap.⁸³ Alternatively, the Developer may use an alternative rate mechanism that may adjust rate recovery through only a reduction in the return on equity and any applicable incentives solely on the amount in excess of the soft Cost Cap.⁸⁴ Importantly, to make use of the latter approach, the Developer's alternative rate mechanism must achieve a rate recovery reduction for the percentage of Included Capital Costs in excess of the soft Cost Cap that is equal to or better for ratepayers in the total long run revenue requirement on a present value basis for the transmission project compared to that which would be achieved under the first approach based on the percentage cost sharing that the Developer proposed to the NYISO.⁸⁵ These tariff and agreement provisions ensure that ratepayers will be protected from cost overruns that exceed a Developer's Cost Cap.

D. Inclusion of Cost Cap in Development Agreement

The NYISO proposes to amend Sections 31.4, 6.10 (Rate Schedule 10), and 31.7 Appendix D (the *pro forma* Development Agreement) of the OATT to require that the Developer's submitted Cost Cap and the excusing conditions be included in the Development Agreement between the NYISO and the Developer of the selected project.⁸⁶ In addition, the Developer must agree in the Development Agreement that it will not seek to recover, through its transmission rates or through any other means, costs for the Included Capital Costs above its agreed-upon Cost Cap, with the exception of the excusing conditions.⁸⁷

This approach is consistent with the approach of other ISO/RTOs. The Commission has accepted other ISO/RTOs' measures to memorialize cost containment commitments proposed by developers in their agreements in a manner equivalent to the NYISO's Development Agreement.⁸⁸ In addition, the Commission has indicated its expectation that the parties to such a development agreement will abide by the terms of that agreement, including the terms concerning cost containment measures.⁸⁹

⁸² Proposed OATT Section 6.10.6.3.

⁸³ *Id.*

⁸⁴ *Id.*

⁸⁵ *Id.*

⁸⁶ Proposed OATT Section 6.10.6.4, 31.4.5.1.8, proposed revision to OATT Sections 31.4.8.3 (revised from 31.4.8.2) and 31.4.12.2.

⁸⁷ Proposed OATT Section 31.4.5.1.8 and 6.10.6.4; proposed revision to OATT Section 31.4.8.3 (revised from 31.4.8.2).

⁸⁸ *See, e.g.,* California Independent System Operator Corp. Tariff, Appx. X Section 10.1.1; Midcontinent Independent System Operator, Inc. Tariff, Att. FF Appx. 1 Sections 9.2; *see also* PJM Interconnection, L.L.C., Order Accepting Proposed Agreement, 154 FERC ¶ 61,054 (2016) (accepting non-standard terms and conditions to an executed PJM designated entity agreement to address a cost containment measure proposed by the selected Developer).

⁸⁹ *See NextEra Energy Transmission West, LLC*, 154 FERC ¶ 61,009 at P 75 n. 129 (2019) ("Regarding CAISO's request concerning the binding nature of the cost caps, we note that NEET West responded by stating that it agreed with CAISO and will not seek to recover any costs incurred above the relevant caps through the Formula Rate. As NEET West and CAISO are both parties to the [Approved Project Sponsor Agreements ("APSAs")] for the Projects, we expect that the parties would abide by the terms set forth and mutually agreed upon in the APSAs.")

i. *Cost Cap Requirements in Development Agreement*

a. General Revisions

The NYISO proposes to revise the *pro forma* Development Agreement for Public Policy Transmission Projects located in Appendix D to Section 31.7 of the OATT to implement the Cost Cap requirements.⁹⁰ Specifically, the NYISO proposes to revise the cost recovery requirements in Article 15.3 of the Development Agreement to provide that a Cost Cap submitted by the Developer will be described in a new Appendix D of the Development Agreement, which description must include the Cost Cap submitted in the Developer's project proposal. The NYISO also proposes to revise Article 15.3 to specify that the Developer agrees to file the Cost Cap for Included Capital Cost with the Commission in accordance with the cost recovery requirements in Rate Schedule 10 of the OATT. The Developer must also agree to implement any soft Cost Cap in accordance with the soft Cost Cap requirements in Rate Schedule 10. The Developer must further agree pursuant to Article 15.3 that it will not seek to recover, through its transmission rate for its transmission project or through any other means, costs of Included Capital Costs above its agreed-upon Cost Cap. Finally, the NYISO sets forth in Article 15.3 the same excusing conditions as contained in Rate Schedule 10 for the recovery of Included Capital Costs.⁹¹

b. Mobile-Sierra Treatment of Included Capital Costs

The NYISO also proposes to include a *Mobile-Sierra* clause in Section 15.3 of the Development Agreement to make explicit the parties' intent to require that the "public interest" standard be met for any changes to the Developer's Cost Cap for the Included Capital Costs and the related provisions in Article 15.3 of the Development Agreement. Specifically, the proposed *Mobile-Sierra* clause states that:

The provisions of this Section 15.3 and the Developer's Cost Cap for the Included Capital Costs detailed in Appendix D shall not be subject to change through application to the Federal Energy Regulatory Commission pursuant to the provisions of Section 205 of the Federal Power Act absent the agreement of all Parties to the Agreement. In any proceeding conducted pursuant to Section 206 of the Federal Power Act, the standard of review for any change to this Section 15.3 and the Developer's Cost Cap for the Included Capital Costs detailed in Appendix D shall be the "public interest" application of the just and reasonable standard set forth in *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956), and *Fed. Power Comm'n v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956), as clarified in *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., Wash.*, 554 U.S. 527

⁹⁰ Proposed OATT Section 31.7, Appendix D.

⁹¹ *Id.*

(2008), and refined in *NRG Power Mktg. v. Maine Pub. Utils. Comm'n*, 558 U.S. 165 (2010).⁹²

Accordingly, the Developer cannot, absent the NYISO's agreement, modify pursuant to FPA Section 205, the Cost Cap for Included Capital Costs or the requirements associated with implementing it in Section 15.3. In addition, the Commission could not modify, on its own motion or on the request of any entity, the Cost Cap for Included Capital Costs or the requirements associated with implementing it in Section 15.3 pursuant to its FPA Section 206 authority unless such a modification is justified under the "public interest" application of the just and reasonable standard.⁹³ Importantly, the *Mobile-Sierra* clause applies only to the Cost Cap for Included Capital Costs, and not the amounts that may be recovered under the applicable Cost Cap. For this reason, it does not guarantee that a Developer will recover the total amount of Included Capital Costs in its Cost Cap or impact the ability of the Commission to review, on its own initiative or at the request of a third party, the prudence of costs incurred below the Cost Cap for Included Capital Costs.⁹⁴

The *Mobile-Sierra* clause in the Development Agreement will provide that the amount of the Included Capital Costs in a Cost Cap will not be modified. The clause ensures that a Developer will not be able to recover costs in excess of the Cost Cap for Included Capital Costs. The clarity about the application of the "public interest" standard will encourage Developers to submit their best offers during the NYISO's process, without having to worry that the Cost Cap for Included Capital Costs, once accepted by FERC, will be subject to potential further revision.

Applying *Mobile-Sierra* doctrine to the *pro forma* Development Agreement is justified by the Commission's precedents on the *Mobile-Sierra* Doctrine. The primary inquiry in determining the eligibility of a particular contract for *Mobile-Sierra* protections is whether the applicable contract provisions are "individualized rates, terms, or conditions that apply only to sophisticated parties who negotiated them freely at arm's length"⁹⁵ The doctrine is based on the "commonsense notion" that in "wholesale markets, the party charging the rate and the party charged [are] often sophisticated businesses enjoying presumptively equal bargaining power, who could be expected to negotiate a 'just and reasonable' rate as between the two of them."⁹⁶

⁹² *Id.* at Section 15.3.

⁹³ The "public interest" application of the just and reasonable standard is set forth in *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956), and *Fed. Power Comm'n v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956), as clarified in *Morgan Stanley Capital Grp., Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., Wash.*, 554 U.S. 527 (2008), and refined in *NRG Power Mktg. v. Maine Pub. Utils. Comm'n*, 558 U.S. 165 (2010).

⁹⁴ For this reason, the NYISO's request for *Mobile-Sierra* protections for the Cost Cap for Included Capital Costs is distinguishable from the request for *Mobile-Sierra* protections addressed by the Commission in *ITC Grid Development, LLC*, 154 FERC ¶ 61,206 (2016). In *ITC Grid Development*, the petitioner sought a declaratory order that would have granted *Mobile-Sierra* protections to the binding revenue requirement bids submitted by the petitioner in various Order No. 1000 processes. This *Mobile-Sierra* protection effectively would have guaranteed the petitioner a defined cost recovery. That is not what the NYISO is proposing here. Rather, the NYISO seeks to protect only the Developer's commitment regarding the Cost Cap for Included Capital Costs.

⁹⁵ *New York Independent System Operator, Inc.*, 162 FERC ¶ 61,107 at P 145 (2018).

⁹⁶ *NRG Power Marketing, LLC, et al. v. Maine Public Utilities Commission, et al.*, 558 U.S. 165 (2010) (citing *Verizon Communications, Inc. v. FCC*, 535 US 467 (2002)).

The Commission’s test for whether arm’s-length bargaining has occurred focuses on two primary criteria. The first criterion is whether the parties to the agreement each have the ability to “negotiate freely” over the provisions for which *Mobile-Sierra* protections are sought.⁹⁷ If a provision in an agreement is presented to a party in a take it or leave it manner, and there is “limited room for negotiation” on the part of one or more of the parties to the agreement, then the agreement is not the product of arm’s-length bargaining.⁹⁸ The second criterion is whether the parties stand in an adversarial posture toward one another over a given issue. An “adversarial negotiation [is one] in which the parties have independent interests and each tries to obtain the best deal for itself.”⁹⁹

The NYISO respectfully submits that the Cost Cap for Included Capital Costs in the Development Agreement satisfies the key prerequisites of being “individualized” and being negotiated at arm’s-length. As an initial matter, the *Mobile-Sierra* clause applies only to the amount of the Included Capital Costs in the Cost Cap, and not to any other provision of the Development Agreement. Furthermore, the terms to be subject to *Mobile-Sierra* protections – the Cost Cap for Included Capital Costs – are “individualized” rather than “generally applicable.” Although the NYISO will pass through to its ratepayers the costs of the applicable project, the Development Agreement, including the Cost Cap for Included Capital Costs, is a bilateral agreement between the Developer and the NYISO. In addition, the Developer is paid directly for the project by the NYISO pursuant to Rate Schedule 10, and not by downstream customers. Thus, the Cost Cap for Included Capital Costs is a contractual commitment that is solely between the NYISO and the Developer.

Furthermore, the Cost Cap provisions in the NYISO tariff provide for Developers to formulate their own Included Capital Costs in an arm’s-length competitive proposal to the NYISO. Given the nature of the NYISO’s process, there is no “take it or leave it” aspect of the pricing proposals. Developers are under no obligation to propose a Cost Cap and, if they elect to propose one, have full latitude to propose a hard Cost Cap or a soft Cost Cap, and to define what cost sharing to propose above the 20% minimum. Developer decisions regarding how and whether to propose a Cost Cap will be driven by competitive considerations – *i.e.*, the knowledge that other Developers are competing for the same project, and that providing a cap that is too high might cause the project to be awarded to a competitor – that are present in all arm’s-length negotiations. The NYISO and the individual Developers bidding on a project each have interests that are independent of and in competition with one another with respect to project pricing. Thus, the process for developing the Cost Cap for Included Capital Costs satisfies the “arm’s-length bargaining” criterion of the Commission’s *Mobile-Sierra* standard. For these reasons, the NYISO respectfully submits that the provisions in the Development Agreement governing the Cost Cap for Included Capital Costs satisfy the conditions necessary for *Mobile-Sierra* protections.

⁹⁷ *Midwest Independent Transmission System Operator, Inc. and the MISO Transmission Owners, et al.*, 147 FERC ¶ 61,127 at P 118 (2014).

⁹⁸ *Id.*

⁹⁹ *Id.* at P 111 (2014) (citing *Santomenno v. Transamerica Life Ins. Co.*, 2013 WL 603901, at 6 (C.D. CA 2013)).

Notwithstanding, if the Commission finds that the *Mobile-Sierra* prerequisites are not fully satisfied here – that is, that the provisions governing the Cost Cap for Included Capital Costs are not “individualized,” or are not negotiated fully at arm’s-length – the NYISO nonetheless requests that the Commission exercise its discretion to grant *Mobile-Sierra* protections to those provisions in the Development Agreement, consistent with *New England Power Generators Association v. FERC*, 707 F.3d 364 (D.C. Cir. 2013) (“*NEPGA*”). *NEPGA* affirmed a FERC order – *Devon Power LLC*, 134 FERC ¶ 61,208 (2011) (“*Devon Power*”) – addressing the applicability of the *Mobile-Sierra* protections to prices derived by the ISO New England Inc. (“ISO-NE”) Forward Capacity Market (“FCM”), as well as to certain FCM transition payments. The NYISO respectfully submits that the circumstances of those provisions in the Development Agreement closely resemble the circumstances that justified the Commission’s exercise of discretion to adopt the *Mobile-Sierra* protections in *Devon Power*. The NYISO’s competitive proposal process relies on market-based mechanisms that “tend to assure just and reasonable rates.”¹⁰⁰ Moreover, as in *Devon Power*, there is a strong need for stability with respect to the Cost Cap for Included Capital Costs agreed to by Developers. The NYISO seek to encourage Developers to bid their best cost containment offers during the NYISO process, an incentive that will be undermined if Developers believe that any Cost Cap for Included Capital Costs that they agree to is subject to revision and/or reduction once they file their rates at the Commission.

Finally, it bear emphasizing that adopting *Mobile-Sierra* treatment will not limit the Commission’s discretion to review the reasonableness of Developers’ costs or the prudence of Developers’ expenditures on Included Capital Costs under the Cost Cap. The *Mobile-Sierra* clause is limited to the Cost Cap requirements, not the entire Development Agreement. Moreover, *Mobile-Sierra* treatment of the Included Capital Costs does not guarantee that a Developer will recover the entire amount of capital costs incurred up to the Cost Cap. Rather, the Cost Cap is a limit on Developer’s recovery of their costs, not a guarantee that they will recover costs that they do not incur or that are not prudently incurred.

ii. Conforming Revisions in Development Agreement

The NYISO proposes to make certain conforming revisions to the Development Agreement concerning the Cost Cap requirements. Specifically, the NYISO proposes to revise the Breach requirements in Article 7.1 of the Development Agreement to provide that a Breach will occur if the Developer fails to file with the Commission its Cost Cap or seeks to recover costs not permitted by the cap, except as permitted for excusing conditions. The NYISO also proposes to revise the Survival requirements in Article 14 to provide that the cost recovery provisions in Articles 15.3 and Appendix D of the agreement will survive termination, expiration, or cancellation of the agreement. This provision is required to give the Developer’s cost containment commitment ongoing enforceability because the Development Agreement will expire once the Developer’s transmission project enters into service, which is the date for the

¹⁰⁰ *Devon Power LLC*, 134 FERC ¶ 61,208 at P 19 (2011).

beginning of cost recovery under the NYISO's tariff unless the Commission determines otherwise.¹⁰¹

E. Other

i. Confidentiality Requirements

The NYISO currently maintains project cost information as confidential information that is not provided publicly.¹⁰² The NYISO proposes to initially maintain as confidential a Developer's proposed total amount of Included Capital Costs and any cost sharing percentage contained in the Cost Cap. If a Developer's project is not found to be viable and sufficient or if the Developer elects not to proceed with a viable and sufficient project, the NYISO will continue to maintain the Developer's Cost Cap information as confidential. If, however, the Developer determines that its viable and sufficient project should proceed to be evaluated for purposes of selection, the NYISO will include the total amount of Included Capital Costs and any cost sharing percentage contained in the Cost Cap in the draft Public Policy Transmission Planning Report that is publicly provided and reviewed by stakeholders.¹⁰³ Disclosing this information about the Developer's cost containment commitment is important to the openness and transparency to all interested parties of information relevant to the Board's evaluation and selection of the more efficient or cost effective project.

V. PROPOSED EFFECTIVE DATE

The NYISO respectfully requests that the Commission accept the proposed tariff revisions for filing with an effective date of February 16, 2020, which the day immediately following the end of the statutory sixty-day notice period for this filing.

VI. REQUISITE STAKEHOLDER APPROVAL

The tariff revisions proposed in this filing were discussed with stakeholders at multiple Electric System Planning Working Group and Transmission Planning Advisory Subcommittee meetings between January and September 2019. At its October 30, 2019 meeting, the Management Committee approved and recommended Board approval of the tariff changes unanimously with abstentions. At its November 19, 2019 meeting, the Board of Directors approved the NYISO making this tariff filing under Section 205 of the Federal Power Act.

VII. SERVICE

The NYISO will send an electronic link to this filing to the official representative of each of its customers, each participant on its stakeholder committees, the New York State Public Service Commission, and the New Jersey Board of Public Utilities. The NYISO will also post the complete filing on its website at www.nyiso.com.

¹⁰¹ OATT Sections 6.10.4.2, 6.10.5.1.

¹⁰² OATT Section 31.4.15.2.

¹⁰³ Proposed revisions to OATT Sections 31.4.11, 31.4.15.2.

VIII. CONCLUSION

Wherefore, for the foregoing reasons, the New York Independent System Operator, Inc., respectfully requests that the Commission accept the proposed tariff changes identified in this filing to provide for the consideration of cost containment in the Public Policy Process.

Respectfully submitted,

/s/ Carl F. Patka

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