

**Order 1000 Narrows the “Right of First Refusal”:
Will Regional Processes be Cost-Effective and Nondiscriminatory?**

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Hypotheticals

To assist readers' understanding of the issues at stake in the right of first refusal area, Allison Clements created three hypotheticals.

1. An incumbent utility in PJM proposes to build a reliability- based transmission project that extends slightly beyond the utility's service territory. PJM realizes that with some modifications, the project could offer, along with the intended reliability benefits, material public policy benefits, by allowing for the importation of more MW of wind from Western PJM to the East. Should the line be modified to accommodate the wind power transport? Who decides? Who should get to build the line? The original utility, or a competing transmission developer willing to do it for less? Should PJM offer up the line for bidding, or should there be some defined process in place to determine who's right it is to build the line? What are the state and FERC roles in resolving these questions?

2. A 150 MW wind farm developer in Oklahoma wants to interconnect to AEP Oklahoma's system and will require a 20 mile interconnection line. After considering the line, SPP determines that some features of the line will increase reliability on not only AEP Oklahoma's system, but also some neighboring transmission systems within the SPP region. Should AEP have the exclusive right to build the interconnection line? What if SPP wants to modify the line to increase the reliability benefits? In that case, should AEP have the right to build or should other transmission developers have a chance to make a proposal about how to build the line? The wind developer's interest is in getting the line built quickly and at lowest cost. Does it/should it have a right to weigh in on its options?

3. Alabama Power wants to build some reliability upgrades in its own service territory. A demand response provider would like to offer an alternative to the utility's desired upgrades, and claims that the alternative could defer the need for some of the utility's upgrades. Is AL Power required to allow consideration of the proposed alternatives, or does it have the right to build its upgrades regardless of outside interest in alternatives? What if it has been demonstrated that the upgrades will benefit neighboring transmission systems? Does the analysis change?

Order 1000 Narrows the “Right of First Refusal”: Will Regional Planning be Cost-Effective and Nondiscriminatory?

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Introduction and Overview

Over 16 years, FERC has issued a series of orders aimed at ensuring cost-effective, nondiscriminatory electric service. Orders 888, 889, 2000, 890, 719, 745 and 755 share a common theme: Alternatives to incumbent-controlled transmission and generation should have opportunities to provide and receive FERC-jurisdictional services (unbundled transmission service and wholesale sales service) under conditions comparable to those enjoyed by incumbent utilities. The latest example of FERC’s insistence is its Order 1000, which “requires each public utility transmission provider to participate in a regional transmission planning process that produces a regional transmission plan.” Para. 68.²

FERC has recognized that transmission owners have incentive and opportunity to use their transmission control and incumbent status to undermine FERC’s principle of comparability. One manifestation of this incentive and opportunity is the federal “right of first refusal” (ROFR) embedded in some FERC-approved contracts and tariffs. The “right” is the incumbent’s right to develop and own transmission facilities deemed necessary to serve the incumbent’s customers, notwithstanding the ability and willingness of non-incumbents to develop those facilities or substitutes for them. Order 1000 requires transmission owners to amend these contracts and tariffs to eliminate the ROFR, where the ROFR applies to projects selected for regional cost allocation. Para. 7. The ROFR still will apply to all other projects. (The common phrase “elimination of ROFR” is not technically accurate. Order 1000 narrows the universe of projects to which existing ROFRs apply, but it does not eliminate the right.)

Underlying FERC’s actions is a double purpose: (1) to eliminate the obstacles to competing proposals erected by the ROFR clauses; and (2) to implement procedures that invite and treat those proposals fairly. With the ROFR thus narrowed, the regions must use comparability and competition to identify cost-effective solutions, both transmission and non-transmission. But merely eliminating the ROFR clauses does not assure that non-incumbent proposals will receive comparable treatment. FERC needed to eliminate not only the *right* of

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² All “para.” cites are cites to Order 1000, unless otherwise indicated.

first refusal but also the *possibility* of first refusal. FERC succeeds with the former but not necessarily with the latter.

This incompleteness produces uncertainties, over how the FERC-narrowed ROFR will affect regional processes. These uncertainties will receive attention during the current discussions over Order 1000 compliance, as well as the ensuing implementation (including FERC rulings on compliance filings and possible Order 1000 revisions). This paper aims to assist clean energy advocates in preparing for these discussions. Those who seek to encourage the entry of non-incumbents, the accommodation of clean power supplies and the cost-effective introduction of non-transmission alternatives, will want to be alert to (a) the types of discretion that incumbents and RTOs can exercise; and (b) legal arguments and actions available to guide that discretion toward comparability and cost-effectiveness. The paper has five sections:

1. *Legal Principles*: How does FERC support its decision to narrow incumbents' right of first refusal?
2. *Boundaries*: What is the legal line between projects for which the ROFR remains and those for which the ROFR is eliminated?
3. *Incumbent Accountability*: What principles and processes will ensure cost-effective decisions?
4. *Obstacles*: For projects seeking regional cost allocation, how might evaluation criteria undermine FERC's ROFR-elimination rule?
5. *Sponsorship*: What are the rights for developers who "win" or "lose"?

An Appendix summarizes the various recommendations.

I. *Legal Principles*: How does FERC support its decision to narrow incumbents' right of first refusal?

The language on which the Commission arises appears in these provisions from Federal Power Act Sections 205 and 206:

Section 205

(a) Just and reasonable rates. All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful. No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

Section 206

(a) Unjust or preferential rates, etc.; statement of reasons for changes; hearing; specification of issues. Whenever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order...

In justifying its ROFR elimination, FERC relies on these provisions for two overlapping rationales:

1. If used to “restrict the universe of competing projects,” the ROFR “may cause the rates, terms or conditions of transmission service to become unjust and unreasonable or unduly discriminatory or preferential.” Para. 283.
2. The ROFR is a “practice” affecting jurisdictional transmission rates, bringing it within Section 206(a). This practice “deprive[s] customers of the benefits of competition in transmission development, and associated potential savings....” Para. 284.

For a third rationale, FERC turns to its general “public interest” responsibilities: The ROFR discriminates against non-incumbent transmission developers. This discrimination is anticompetitive. The statute’s “public interest” phrase reflects “an overriding policy of maintaining competition to the maximum extent possible consistent with the public interest.” Para. 285 (*quoting Otter Tail Power Co. v. United States*, 410 U.S. 366 at 374 (1973)). The Commission therefore “has a responsibility to consider anticompetitive practices and to eliminate barriers to competition.” Para. 285 (*citing Gulf States Utils. Co.*, 5 FERC P61,066 at 61,098 (1978)). With this reasoning, FERC explicitly rejects incumbents’ arguments that the Act’s antidiscrimination provisions protect only consumers, and not competitors. Para. 285.

The distinct statutory phrases “just and reasonable” rates and “no undue preference” support FERC’s regional transmission planning goals in the following ways:

Just and reasonable: A failure to consider “more efficient or cost-effective solutions” could result in solutions that are higher cost than necessary, violating the just-and-reasonable

principle. Those higher costs could be transmission costs, power supply costs, or both. Para. 254 states: “By requiring the comparable evaluation of all potential transmission solutions, the Commission has sought to ensure that the more efficient or cost-effective solutions are in the regional transmission plan.” Since the purpose of transmission is to transmit electricity to load, “cost-effective solutions” refers not to transmission cost alone but to the combination of transmission cost and wholesale power cost. Cost-effective transmission, therefore, is transmission that (a) itself reflects prudent costs, and also (b) accommodates wholesale power that is cost-effective. Comparing the cost of two separate transmission lines in isolation could produce the wrong answer if one line costs more than the other but would accommodate, over a given number of years, more lower-cost power than the other to displace higher-cost power.

Nondiscrimination: Nondiscriminatory rates and practices treat similar customers similarly and dissimilar customers dissimilarly. FERC here has expanded the protected interests to include not only customers but also alternative transmission suppliers and competing sources of supply:

“[I]t is not in the economic self-interest of public utility transmission providers to expand the grid to permit access to competing sources of supply. In Order No. 890, the Commission required greater coordination in transmission planning on a regional level to remedy the potential for undue discrimination by transmission providers that have an incentive to avoid upgrading transmission capacity with interconnected neighbors where doing so would allow competing suppliers to serve the customers of the public utility transmission provider.”

Para. 253. The incumbent can use its control over the design, selection, and construction processes to favor its own business strategies. Those strategies include as blocking competitors from reaching its customers; adding to rate base instead of purchasing from others; incurring transmission or generation costs that, once sunk, make demand response or energy efficiency uneconomic; and creating transmission paths that give its generation surplus a competitive advantage in wholesale markets. The likelihood of this abuse is lowered if non-incumbent transmission developers have a comparable opportunity to offer projects, and to have those projects considered on equal terms.

FERC views ROFR elimination as necessary to both results: just and reasonable rates, and nondiscriminatory rates and practices:

“Just as it is not in the economic self-interest of public utility transmission providers to expand transmission capacity to allow access to competing suppliers, it is not in the economic self-interest of incumbent transmission providers to permit new entrants to develop transmission facilities, even if proposals submitted by new entrants would result in a more efficient or cost-effective solution to the region’s needs. We conclude that an incumbent transmission provider’s ability to use a right of first refusal to act in its own economic self-interest may discourage new entrants from proposing new transmission projects in the regional transmission planning process.”

Para. 255.

II. *Boundaries: What is the legal line between projects for which the ROFR remains and those for which ROFR is eliminated?*

A. In general

Under Order 1000, the legal line between (a) projects for which the incumbent retains the ROFR, and (b) projects entitled to comparable consideration regardless of incumbent preference, is drawn by the project's selection for regional cost allocation. See Para. 7 (explaining that the ROFR-removal requirement "applies only to transmission facilities that are selected in a regional transmission plan for purposes of cost allocation"). If an incumbent utility chooses to recover the costs of its intra-service territory project from its service-territory customers only, then its right of first refusal, with respect to that project, is unaffected by Order 1000. This conclusion is based on several Order 1000 statements:

Para. 63 (defining "local transmission facility" as "a transmission facility located solely within a public utility transmission provider's retail distribution service territory or footprint that is not selected in the regional transmission plan for purposes of cost allocation").

Para. 7 (explaining that ROFR elimination does not apply to "transmission facilities in local transmission plans that are merely 'rolled up' and listed in a regional transmission plan without going through an analysis at the regional level, and therefore, not eligible for regional cost allocation").

Para. 225 (explaining that FERC is "focus[ing] on the set of transmission facilities that are evaluated at the regional level and selected in the regional transmission plan for purposes of cost allocation, and not on transmission facilities included in local transmission plans that are merely 'rolled up' and listed in a regional transmission plan without going through a needs analysis at the regional level (and therefore, not eligible for regional cost allocation)...").

Some confusion can arise over terminology, especially the terms "service territory" and "footprint." Both Order 1000 and its associated Notice of Proposed Rulemaking (131 F.E.R.C. P 61,253 (2010)) use the terms, but neither document defines them. Based on common usage and context, I believe FERC intends the following definitions:

"Service territory" means the area defined by state-prescribed boundaries within which an incumbent utility has an obligation to serve.

"Footprint" is the area within which an RTO is the "public utility" (as defined by the Federal Power Act) providing transmission service. That area, in turn, consists of the combined service territories of the transmission-owning utilities that have transferred control of their transmission assets to the RTO.

B. How does the boundary line apply to reliability projects, generator interconnection projects, and “participant-funded” projects?

Since the dividing line for ROFR elimination is a project’s selection in a regional plan (and therefore eligibility) for purposes of regional cost allocation, any of the three types of projects could land on either side of the line.³

1. Reliability projects

A reliability project could be eligible for regional cost allocation, whether proposed by a non-incumbent or incumbent. As with any project, eligibility depends on whether the project will produce regional benefits sufficient to merit inclusion in the regional plan for purposes of cost allocation. And a reliability project could be eligible for regional cost allocation even if it is located entirely within an incumbent’s service territory, as para. 261 demonstrates:

“261. ... Currently, an incumbent transmission provider may meet its reliability needs or service obligations by building new transmission facilities that are located solely within its retail distribution service territory or footprint. The Final Rule continues to permit an incumbent transmission provider to meet its reliability needs or service obligations by choosing to build new transmission facilities that are located solely within its retail distribution service territory or footprint and that are not submitted for regional cost allocation. Alternatively, an incumbent transmission provider may rely on transmission facilities selected in a regional transmission plan for purposes of cost allocation. Our decision today does not prevent an incumbent transmission provider from continuing to propose transmission projects for consideration in the regional transmission planning process and to receive regional cost allocation if those projects are selected in a regional transmission plan for such purposes, even if they are located entirely within its retail distribution service territory or footprint.”

This language implies that a non-incumbent could (a) propose a project that lies solely within a single utility’s service territory, (b) assert that the project’s regional benefits warrant its selection for regional cost allocation, and then (c) have it compete head-to-head with the incumbent’s intra-service territory project envisioned in the last sentence of para. 261. The utility would have no right to first refusal, if it has sought regional cost allocation. In contrast, if the incumbent is not seeking regional cost recovery for its intra-service territory reliability project, it retains its ROFR regardless of the non-incumbent’s competing proposal. The

³ In discussing regional cost allocation, there is some confusion about the terms “eligibility” and “selected.” Although some use these terms interchangeably, they are not synonyms. Para. 334 explains the relationship: “[E]ligibility for regional cost allocation is tied to the transmission facility’s selection in the regional transmission plan for purposes of cost allocation and not to a specific sponsor.” In other words, “selection” is the prerequisite for “eligibility,” while “eligibility” means eligibility for regional cost allocation.

incumbent's project will, of course, still be subject to a prudence review by the relevant rate regulator, a subject discussed in Part III below.

2. Generator interconnection projects

Brief background: In Order 2003, FERC made interconnection service a component of transmission service, bringing it under the nondiscrimination requirements of Order 888. An incumbent transmission owner therefore must treat non-incumbent generator interconnection requests on a basis comparable to the way in which the incumbent treats its own interconnection needs.

Turning to the ROFR: In the case of both reliability projects and generation interconnection projects, if an incumbent utility needs to develop an interconnection facility solely within its service territory and does not seek regional cost allocation, it can use its right of first refusal. If a non-incumbent wishes to propose an interconnection project as a substitute for the utility's interconnection project (or as a substitute for a utility transmission project for which the utility is not going to seek regional cost allocation), the non-incumbent faces an entry barrier because the utility's ROFR allows it to ignore the non-incumbent. In this situation, the non-incumbent could argue to the state commission (and the affected RTO) that the utility's project is imprudent, because the non-incumbent's substitute is lower in cost relative to the incumbent utility's ratepayers—either because project costs are lower or because the non-incumbent could show regional benefits and thus spread over a large number of customers the interconnection costs that the incumbent utility would be imposing entirely on its captive customers. If the incumbent provides transmission service to wholesale customers (that service is FERC-jurisdictional), the non-incumbent could make the same argument to FERC, and to the RTO in RTO regions.

3. Participant-funded projects

Definition: A participant-funded project is a project that does not carry out an obligation to serve; its purpose is entrepreneurial. Its financial support comes from the voluntary buyers and sellers of the power to be transported by the project, not from captive customers paying regulated rates. This category therefore excludes incumbent projects designed to carry out an obligation to serve, as well as non-incumbent projects proposed as substitutes for such incumbent projects. Conversely, a participant-funded project could be sponsored by an incumbent for a location outside its service territory, or by a non-incumbent anywhere; the common feature is that it would not have the financial certainty of regulator-mandated cost recovery.

Whether existing ROFRs apply to a participant-funded project sponsored by an incumbent depends on the wording of ROFR provisions in existing tariffs. I doubt that the existing ROFR provisions apply to an incumbent's participant-funded projects, because the purpose of ROFRs is to give the incumbent superior rights to determine how to serve its obligatory load.

What if a non-incumbent, participant-funded project seeks to substitute for an incumbent-funded project? Because the participant-funded project is self-funded, it is not seeking regional cost allocation. But that fact alone does not mean a regional planning process should ignore it. The regional planning process should focus on selecting the best mix of projects, regardless of how funded. Compliance filings should make this point clear, especially those filings from non-RTO regions, because they have lacked a formal procedure for comparing options. Further, while Order 1000 itself does not provide a challenge path for a participant-funded project ignored or rejected by the regional process, that project should have an opportunity to challenge its non-selection, either directly through a complaint to FERC, or indirectly by challenging the prudence of expenditures associated with the selected project, as discussed under “Generator interconnection projects” above.

III. *Incumbent Accountability: What principles and processes will ensure cost-effective decisions?*

A. Overview

The decision-making process faced by a project proposal will vary with three factors: whether the ROFR applies, whether the region is an RTO region, and whether the transmission costs at issue are bundled (making them state-jurisdictional) or unbundled (making them FERC-jurisdictional). Despite these variations, the following principles are, or should be, common to all the scenarios:

1. Rates must be just and reasonable.
2. Just and reasonable rates require prudent costs and prudent practices to incur those costs.
3. The right of first refusal does not exempt a utility from the prudence requirement, because its rates must be just and reasonable.
4. Prudence requires cost-effectiveness relative to all feasible alternatives.⁴

⁴ There is no ambiguity about FERC’s obligation to apply the prudence standard, notwithstanding the occasional inaccurate comment that “FERC doesn’t do prudence reviews; states do.” The statute requires FERC to ensure just and reasonable rates. The purpose of that standard is to protect the consumer from inefficiency and waste. In the context of transmission projects controlled by incumbent, vertically integrated companies, there are two reasons for prudence alertness. First, transmission is a monopoly asset, so there is not a competitive market to provide benchmarks against which to judge the monopoly’s cost performance. Second, transmission is a strategic asset that the incumbent can deploy to protect its generation from competition. Protecting the consumer from imprudent costs is a regulatory obligation that attaches to those transactions subject to the regulator’s jurisdiction: for states, retail rates; for FERC, unbundled transmission service and the sale of electric energy at wholesale. How to assess prudence is a subject of fair debate. Whether to assess prudence is not.

5. A prudent means of determining all feasible alternatives is to have an open process with common deadlines and evaluation criteria. Competitive bidding has these features.
6. Relying on a contestant to design the competition and/or judge the results is an ineffective way to determine the most cost-effective alternatives.
7. Information about whether an ROFR exists for a particular project should be available sufficiently early in the planning process so that non-incumbents who compete for a slot avoid the risk of disclosing their data and analyses only to have the incumbent use that information for its own project.

This section now applies these principles to the RTO and non-RTO contexts.

B. RTO regions

In RTO regions, the RTO can help ensure prudence by using a process that stimulates and evaluates alternative means of satisfying the region's needs cost-effectively. The process should—

1. identify all needs in the region (both local and regional); then
2. create alternative regional plans that take into account all of the following: (a) regional projects eligible for regional cost allocation, (b) incumbent local projects subject to the residual ROFR, and (c) non-incumbent regional projects that could substitute for incumbent-proposed local projects.

This approach requires the utility to announce that it is considering a project, well before the time when groundbreaking must occur. (The announcement should occur before, not after, the utility has done studies and used up the time period that non-incumbents would need to design projects in time for their consideration.) The RTO then would invite proposals for alternatives, assess their relative costs and benefits, and deliver a non-binding, neutral opinion. It is important here to distinguish between (a) “truly local” projects, i.e., projects which are so “local” that there could never be a regional substitute for them; and (b) projects initially conceived by the incumbent as local, but susceptible to being replaced, or made unnecessary, by a regional project, including a non-transmission alternative with regional benefits. While there is no need for the RTO to be involved in the first category, it should remain open to considering proposals in the second category.

The process also could include a formal competitive bidding procedure, to inject neutrality and reduce subjectivity in the evaluations.

This process would produce evidence that FERC and state regulators can use to assess the prudence of incumbents' local proposals, since the prudence standard requires selection of the most cost-effective alternatives. Exposed to this information, an incumbent will be less likely to use its ROFR to block better projects. Note also that absent an RTO-conducted

evaluation, each regulator (FERC and affected states), to apply the prudence standard conscientiously, would have to carry out this same type of process (i.e., comparing its local utility's proposal to all feasible alternatives). The RTO process therefore reduces regulatory workload—a benefit to both regulators and project proponents.

Relying on the RTO also has disadvantages. The assumption is that an RTO process would give no planning or presentational advantages to the incumbent transmission owners. But that assumption is not necessarily consistent with a specific RTO situation. An RTO still can have institutional preferences for transmission over non-transmission solutions, simply because the RTO's personnel understand them better and can control their operation more readily. Further, the RTO is a voluntary organization whose transmission-owning members can depart if they feel the RTO pays them insufficient deference. When these disadvantages exist, the better approach is for the RTO to use an independent entity to develop the criteria and evaluate the projects.

C. Non-RTO regions

In the non-RTO regions, the prudence standard still requires the comparison to alternatives, but the procedures for making this comparison neutrally are less obvious since there is no RTO. It will not work to rely on studies carried out by incumbents; there is too much risk of back-scratching (i.e., each incumbent assenting to each other incumbent's project), or the opposite (critiques and delays mounted against one incumbent by another competing incumbent). To comply with Order 1000's "comparable treatment" requirement, the region's utilities should use an independent entity for the assessment process. The independent entity would guide the conversations, evaluate the incumbents' and non-incumbents' proposals, and carry out the assessments, using procedures similar to those described in the RTO context above.

On this point, the Commission has not yet been helpful. See para. 229:

"...The Commission declines, however, to mandate the use of independent third-party observers, as suggested by Western Independent Transmission Group. To the extent public utility transmission providers in consultation with other stakeholders in a region wish, they may propose to use an independent third-party observer and we will review any such proposal on compliance."

In this respect the Commission errs, no less so than did FERC in letting several decades of transmission discrimination go by before deciding, with Order 888 in 1996, to require nondiscriminatory access to incumbent transmission service. Discrimination, through planning controlled by the incumbent, is no less likely or problematic than is discrimination through access and pricing.

D. Consequences for non-compliance

What actions should FERC take, or commit to take, so that a culture of neutrality and objectivity prevails? As with Order 1000 generally, FERC does not state the consequences for an incumbent who behaves improperly. While the tariffs required by Order 1000, once approved by FERC, will establish frameworks, regulators must make clear the consequences for violators of those frameworks. Here are some options, for RTOs, state regulators, and FERC, with which to address situations where the incumbent proposes a project in a context where there has been insufficient opportunity and process for multiple, well-funded competitors to compete to meet identified grid needs:

1. Eliminate any existing presumption of prudence for, or regulatory deference to, an incumbent's proposed project.
2. Reject the proposal, then create an opportunity for non-incumbents to compete to carry out the incumbent's proposal (subject to their paying the costs incurred by the incumbent to create the proposal).
3. Allow the proposal, but assign financial consequences, where permitted by law, such as (a) reduction in the utility's transmission return on equity; (b) direct financial penalty; (c) for FERC, revocation of affiliate's authority to charge market-based rates; and (d) disallowance of project costs to the extent they exceed the cost of the most cost-effective alternative.

E. Application to a likely scenario

What if an incumbent utility has a "local" (i.e., intra-service territory) project that is ineligible for regional cost allocation, but a non-incumbent wishes to propose a project that can both (a) substitute for that incumbent project and (b) provide regional benefits that make it eligible for regional cost allocation? Does the incumbent have an Order 1000 obligation to consider this non-incumbent project in a manner comparable to its own project, notwithstanding its right of first refusal?

The right of first refusal is the incumbent's right to build, own, and operate a project notwithstanding the availability of a non-incumbent's project. The right relieves the incumbent of an otherwise-existing, Order 1000 obligation to consider alternatives comparably. In other words, the incumbent will not have committed undue discrimination (at least in the view of Order 1000) by ignoring the non-incumbent project. But an incumbent's right to own and operate its own project does not relieve it of its obligation to charge only just and reasonable rates, including making prudent decisions when incurring the costs that support those rates. So where an incumbent insists on building its own local project when a non-incumbent's solution could produce comparable benefits at lower cost, FERC (or the state, if the transmission costs are retail bundled costs) should disallow the excess costs.

Given this reasoning, FERC should both (a) make this prudence point explicit so that objectors don't face later incumbent arguments that their right of first refusal shields them from

prudence review, and (b) condition any presumption of prudence—and any finding of justness, reasonableness and nondiscrimination—on the incumbent’s having used neutral competitive bidding processes to identify alternatives to their own projects that could produce the intended benefits at lower cost. This requirement does not eliminate the right of first refusal, because if alternative projects do no more than match the incumbent’s option, the incumbent still wins. But it does align the right of first refusal with the prudence obligation.

F. Can a “bottom up” planning process ensure comparability and objectivity?

Some have proposed a “bottom up” regional planning approach that (a) allows each incumbent transmission provider to create an independent plan focused on its own customers, (b) compiles and coordinates these plans, and then (c) reactively considers any alternatives proposed to in response to this compilation. Would this approach satisfy Order 1000’s insistence on objective, comparable consideration? Would it produce the most cost-effective mix of projects, along with a record verifying that outcome as sufficient to persuade regulators that the costs were prudent and the resulting rates just and reasonable?

As for Order 1000, the answer, at least for now, could be “yes,” depending on the design. Para. 254 allows what FERC calls a “bottom up, top down” approach. This is not a mere stapling together of local plans, where alternatives would have no chance to emerge. (That is why FERC uses the term “bottom up, top down,” rather than merely “bottom up.”) FERC wants the approach to allow for the “comparable evaluation of all potential transmission solutions.”

The question is whether a process that delays the consideration of alternatives to incumbent control until the incumbents have submitted their proposals can ensure comparable treatment. I would argue no. A respondent is never in the same position as the initial actor, who has the power to frame the question, assign internal resources to its proposed answer, and run the clock, so that there are insufficient time and resources to consider alternatives before the necessary date of groundbreaking. Here is a way to combine the concepts of “bottom up” and “top down” to ensure comparability and objectivity. There are three premises and then several possible actions.

1. Three premises

a. The purpose of transmission facilities is to bring retail consumers the electricity they demand most cost-effectively.

b. The entities with the legal obligation to provide retail consumers with the electricity they demand are the retail load-serving entities (and wholesale load-serving entities, to the extent that they have contractual wholesale customers like municipal and cooperative systems).

c. The specifics of each retail load-serving entity’s obligation to serve are determined (or should be determined) by state commissions carrying out state legislative commands by issuing orders to their utilities.

2. Actions

Given these premises, the process should start by specifying the needs of each load-serving entity. That specification should come from the states, or from each state's load-serving entities acting subject to the state commission's orders. In effect, the initial movers would be the state commissions, who determine that mix of generation, transmission, distribution, conservation, storage and other resources that best serves their citizens. *It is important for states to restore, and modernize, utility-specific integrated resource-planning processes so as to produce a clear statement of those states' needs and preferences and thereby frame the regional discussions for their citizens. The absence of such plans is the single most important reason why some states feel, or are, ignored in the regional discussions.*

Once those state power-supply preferences (in terms of load levels and power-supply mixes over some time period) are clear, two possible paths emerge. (At this point in the process, no "transmission plan" has emerged from an incumbent; what have emerged are state-specific preferences for the power-supply mix.)

1. The more logical path is a regional process that, through objective analysis, produces that mix of transmission and non-transmission projects that will most cost-effectively connect the most economic sources for the desired power mix with the specified loads. In the pre-regional-markets days, that is what each utility did within its own service territory: plan transmission to connect resources with loads. Order 1000 creates an opportunity to perform this action at the regional level.
2. The less logical path, once the states have specified their consumer preferences, is for each incumbent to create its own service-territory-centered transmission plan, ignorant of what every other transmission provider is doing; then review the full set of transmission plans together to identify and correct the inevitable conflicts, gaps, and redundancies. With every incumbent (and state) focused on defending and advancing its specific transmission project, there is risk of missing cost-effective regional solutions, as well as solutions that allow non-incumbent competitors to offer alternatives. This path, even if it complies technically with Order 1000, will not serve regions well.

IV. Obstacles: For projects seeking regional cost allocation, how might evaluation criteria undermine FERC's ROFR-elimination rule?

Where a project is included in a regional plan as a cost-effective solution to a given need, Order 1000 allows its cost to be allocated across that region. This cost-allocation right must be comparable for incumbent and non-incumbent transmission providers.

Comparable treatment, however, does not require identical treatment, says para. 323. Approaches may vary across regions, but within regions comparable treatment remains the rule.

Yet even within a region the same requirements may affect incumbents and non-incumbents differently because state law treats them differently. The question is whether those differences produce unjust and unreasonable rates or undue discrimination. If so—if comparable treatment leads to unlawful results—adjustments will be necessary.

A. Site readiness

The problem will arise where regions seek to require non-incumbents to demonstrate one or more of eminent domain power, site control, or right-of-way control, before their projects will receive consideration for inclusion in a regional plan for purposes of cost allocation. Since these three criteria raise common issues and have a common purpose—readiness—I will refer to them together as “site readiness,” except where there is a discussion unique to one of them.

There are two related questions: First, are these requirements true indicators of project merit or are they created to disadvantage non-incumbents? Second, where these requirements are true indicators of project merit, do they affect incumbents and non-incumbents comparably or is there an inadvertent disadvantage to non-incumbents? For example, does the non-incumbent have to take extra steps to achieve the same qualification, adding more time and delay and therefore making its option suffer in comparison? Consider these examples:

1. What if the process requires a project developer to have state law “public utility” status at the time of project proposal, such that the likely multi-month commission process required to obtain that status will make the non-incumbent miss the application deadline? Besides the deadline problem, the non-incumbent developer might have incurred the state procedure costs pointlessly if its project is not chosen. If these requirements are unrelated to project readiness, they become an inappropriate basis for incumbents’ avoidance of the ROFR elimination rule.
2. Another example is requiring site control earlier than is necessary to show site readiness, merely because incumbents already have it (due to their past obligation to serve) and non-incumbents don’t.
3. A third example is that state statutes tend to grant eminent powers only to incumbent utilities with retail obligation to serve.

If these factors are available differentially to incumbents for reasons other than merit, they become obstacles to a non-incumbent’s selection that translate into undue discrimination or unjust and unreasonable rates. If these indicators are related to project readiness, there is a need to identify workarounds that enable non-incumbents to qualify, rather than accept the competitive distortions that would result.

These problems are solvable, but not if regions favor incumbents by rotely applying legacy state law. The solution is for incumbents to share their resources with, or exercise their state law powers on behalf of, the non-incumbent in whatever way is necessary to get the non-

incumbent equivalent access to the state law benefit. In this respect, site readiness is analogous to the transmission control that led FERC to promulgate Order 888. FERC there recognized that transmission access was necessary to generation competition. Because transmission access was controlled by incumbents, FERC ordered them to share. Site readiness is essential for transmission competition. Therefore, incumbents need to share their unique powers to obtain site readiness.

Applying this principle: Where particular land is necessary for a transmission project, and where access to that land is differentially available to the incumbent because of its pre-existing ownership (funded by captive ratepayers) or eminent domain powers, the principle of nondiscrimination requires the incumbent to make the land available to a non-incumbent project that, but for the absence of site control, would be eligible for regional cost allocation. That is, if it is unique land that the incumbent already controls, FERC should require the incumbent to make the land available to the non-incumbent. If it is land not yet controlled by the incumbent but available to the incumbent on exercise of its eminent domain powers, FERC should require the incumbent to exercise its eminent domain powers on behalf of the non-incumbent's project (or commit not to exercise its eminent domain powers on its own behalf). These requirements should be conditions on the incumbent's retention of the remaining right-of-first-refusal left intact by Order 1000. Then, given this incumbent obligation, the qualifications process should assume the non-incumbent to have site control.

(Caution: Not all site-control situations inherently favor the incumbent. Only when the incumbent already has control of a uniquely valuable site, or where it obtained that control through use of captive ratepayer funds, and where the non-incumbent cannot itself realistically acquire a comparable site, is there a non-merits advantage in the incumbent.)

While Order 1000 does not bar these solutions, it leaves the problem unaddressed. Para. 324 requires a region's qualification criteria to "allow any transmission developer the opportunity to remedy any deficiency" but fails to address the real problem: where the "opportunity to remedy any deficiency is controlled by the incumbent." Footnote 303 (accompanying para. 324) says that nothing precludes an incumbent from contracting with non-incumbents, but it does not require them to do so.⁵ Similarly, para. 225 states that Order 1000 is not intended to "alter an incumbent transmission provider's use and control of an existing right of way." See also para. 318 ("[T]his Final Rule does not ... grant or deny transmission developers the ability to use rights-of-way held by other entities, even if transmission facilities associated with such upgrades or uses of existing rights-of-way are selected in the regional transmission plan for purposes of cost allocation. The retention, modification, or transfer of rights-of-way remains subject to relevant law or regulation granting the rights-of-way.").

⁵ Note 303 provides: "The Commission notes, however, that nothing in the qualification requirement of this Final Rule precludes a transmission developer from entering into voluntary arrangements with third parties, including any interested incumbent transmission provider, to operate and maintain a transmission facility. Similarly, nothing in this Final Rule creates an obligation for an incumbent transmission provider to operate and maintain a transmission facility developed by another transmission developer...."

A fair interpretation of the statute's two key phrases should convert the incumbent's option into an obligation. Consider:

Just and reasonable rates: For the incumbent's rates to be "just and reasonable," the underlying costs must be prudent. If the utility has state law power to use its eminent domain authority to assist a non-incumbent project, and the non-incumbent project will reduce the incumbent's cost of serving its customers, then the utility that fails to assist deserves a prudence disallowance, or at least a denial of the presumption of prudence; meaning that it must show that its refusal to assist was prudent. FERC's "just and reasonable" duty requires the disallowance. In this prudence context, FERC's authority is not to require the incumbent to assist the non-incumbent, but to disallow excess costs attributable to the incumbent's refusal to assist. Also note that this prudence-disallowance consequence exists only if the incumbent's inaction inflates its own cost to serve. If the non-incumbent project requiring the incumbent's assistance would reduce only regional costs but not the incumbent's costs, there would be no incumbent rate case where FERC could disallow the incumbent's excess costs. In its orders accepting tariffs that retain the incumbent's discretion to refuse assistance, FERC should make clear that it is preserving its authority to disallow imprudent costs arising from these situations.

No undue preference: An incumbent that exercises eminent domain for its own projects but not for others engages in a "practice" affecting rates that is unduly preferential, in violation of Section 206(a). Order 1000 does not make this precise point, but Order 2003 does. Order 2003 made "interconnection service" part of "transmission service" subject to Order 888's "golden rule": Each transmission owner must provide interconnection service to others on terms comparable to the way the owner provides the service to itself. FERC there viewed eminent domain power as sufficiently important to nondiscriminatory transmission service to require the incumbent to exercise it nondiscriminatorily. See para. 251 of Order 2003, and Article 5.13 of the Large Generator Interconnection Agreement attached to Order 2003:

"251. ... [I]n the Final Rule, ... [LGIA Article 5.13], Lands of Other Property Owners, we require that a Transmission Provider or Transmission Owner use efforts similar to those it typically undertakes on its own behalf (or on behalf of an Affiliate), which may include use of eminent domain rights, to secure permits for the Interconnection Customer, unless restricted from doing so by state law."

"5.13 Lands of Other Property Owners. *If any part of the Transmission Provider or Transmission Owner's Interconnection Facilities and/or Network Upgrades is to be installed on property owned by persons other than Interconnection Customer or Transmission Provider or Transmission Owner, the Transmission Provider or Transmission Owner shall at Interconnection Customer's expense use efforts, similar in nature and extent to those that it typically undertakes on its own behalf, including use of its eminent domain authority, and to the extent consistent with state law, to procure from such persons any rights of use, licenses, rights of way and easements that are necessary to construct, operate, maintain, test, inspect, replace or remove the Transmission Provider or Transmission Owner's Interconnection Facilities and/or Network Upgrades upon such property. Upon receipt of a reasonable siting request, Transmission Provider shall provide siting*

assistance to the Interconnection Customer comparable to that provided to the Transmission Provider's own, or an Affiliate's generation."⁶

Order 2003's reasoning applies here. An incumbent's use of unique eminent domain power for its own projects but not for others is undue discrimination. FERC's omission of this statement is an error. It becomes a legal error if someone seeks this benefit from a utility, the utility denies it (while reserving the eminent power for itself), and FERC upholds the denial.

Note: Under Section 216 of the Federal Power Act, it is possible for developers who lack eminent domain powers under state law to obtain it from FERC. But Section 216's detailed, multi-step process is in no way comparable to the incumbent's ability to use its own state-law power of eminent domain. Section 216 requires the applicant to obtain (a) from the U.S. D.O.E., a designation of the project's location as within a "national-interest electricity transmission corridor"; and (b) from FERC, a preemptive eminent domain permit. But the applicant must seek state permission before approaching FERC; and, under the Fourth Circuit's interpretation of Section 216, the state can oust FERC's jurisdiction by denying the applicant's request within 12 months. *Piedmont Environmental Council v. FERC*, 558 F.3d 304 (4th Cir. 2009). The incumbent need not go through these steps.

Note that the right-of-way situation raises the same comparability questions as site control does; right-of-way control is a feature of readiness. The main difference is one of timing. An existing right-of-way is already incumbent-controlled; land subject to the incumbent's power of eminent domain is not yet, but inevitably, incumbent-controlled. If the land is indispensable to economical market entry by a non-incumbent, the incumbent's denial of access is inconsistent with the just-and-reasonable standard (to the extent it deprives customers of a lower-cost option relative to the incumbent's offerings), as well as the

⁶ The D.C. Circuit upheld the provision as within FERC's authority:

"We recognize that a state's authority to exercise the eminent-domain power, and to license public utilities to do so, is an important state power. But FERC has done nothing more than impose a nondiscrimination provision on public utilities. The orders explicitly leave state law untouched, specifying that any exercise of eminent domain by a public utility pursuant to the orders' nondiscrimination mandate be 'consistent with state law.' Order No. 2003-A at 31,144, LGIA sec. 5.13; see also *id.* at 31,004 P 300. Thus the states remain completely free to continue licensing public utilities to exercise eminent domain, or to discontinue that practice. To be sure, if hitherto a utility would not have exercised eminent domain to enable interconnection with an independent generator, the orders, conditionally, compel the utility either to broaden its use of the state-provided authority for the benefit of independents, or to drop the use for its own and its affiliates' power. But the modifier *conditionally* is critical. Nothing in the federal rule compels either continued state retention of the license, or public utilities' continued employment of eminent domain...."

National Ass'n of Regulatory Utility Comm'rs v. FERC, 475 F.3d 1277, 1283 (D.C. Cir. 2003).

prohibition against undue preference. It is also potentially inconsistent with antitrust law, although that conclusion depends on facts and, under the state action doctrine, the nature of the incumbent’s state-law rights to the right of way.

B. “Public utility” status

Some states reserve “public utility” status for entities that have a state-law obligation to serve, a category that excludes non-incumbent transmission developers. Other states apply “public utility” status to a broader universe of entities, such as all entities providing or transporting electricity. Depending on the state law’s purpose, public utility status can be essential to non-incumbents but unavailable, such where it is a prerequisite for exercising eminent domain powers but available only to entities having an obligation to serve. Or, the status might apply to non-incumbents (because of their providing some type of electric service), but involve intensive regulatory oversight, some of which is appropriate for non-incumbents (such as safety) but others of which seem relevant only to incumbents with captive customers (such as cost reporting—which, for non-incumbents, would not be relevant to states, since the unbundled transmission service provided by a non-incumbent is exclusively FERC-jurisdictional).

The regions therefore should not include public-utility status as a criterion unless that status is germane to a project’s merits and there is no other way to replicate those merits—such as the actions discussed above under “Site readiness.” Otherwise, there is risk of regions’ using the public utility status screen arbitrarily to exclude non-incumbents. If, for example, a region’s intended purpose of a public utility status criterion is—

1. to ensure eminent domain powers, the status is unnecessary if the incumbent can exercise its powers on the non-incumbent’s behalf.
2. to ensure sufficient financial scrutiny, the region can achieve this goal independently of state-commission review by creating financial strength factors in the qualifications criteria.
3. to ensure safety compliance, the region can create its own criteria and methods rather than subject the entity to multiple state-based reviews.

C. Regional cost allocation for non-transmission alternatives

FERC has focused on ensuring the availability of regional cost allocation for non-incumbent providers of transmission alternatives. Might its reasoning support regional cost allocation for non-transmission alternatives, like energy storage?

To clarify terminology: In my March 2012 paper on non-transmission alternatives,⁷ I distinguished three categories:

1. conventional transmission (poles and wires);
2. “ancillary services” (mostly generation services, defined in Order 888 and also discussed in Order 755—services that Order 888 deems to be “transmission” because they are essential to the stability of transmission service); and
3. non-transmission alternatives (which, by definition, are not “transmission” and thus are not, at least technically, subject to FERC’s jurisdiction; an example is demand response, although one can imagine situations where these services can act as ancillary services).

If the service fits into the ancillary service category, it is “transmission” and therefore can qualify for regional cost allocation. If not (i.e., if the service fits into neither of FERC’s jurisdictional service categories—transmission of electric energy and sale of electric energy at wholesale), there is no direct path by which FERC can order allocation of the costs. FERC can allocate only the costs of a jurisdictional service. The fact that a service can substitute for transmission service does not make it transmission service. It is true that if transmission projects are eligible for regional cost allocation but substitutes for those projects are not, the competition between these two options is distorted. But the distortion arises from the limits on FERC’s jurisdiction, not because of any action or omission by a market actor. For that reason, terms like “unduly preferential” and “anticompetitive” would not apply.

There is, therefore, no direct path to allocate regionally the cost of a non-jurisdictional service. But if we alter the concept slightly, talking not of “non-jurisdictional service” but instead of “inputs to a jurisdictional service,” there is a possible path to allocating the cost regionally. FERC derives jurisdictional transmission rates using the traditional revenue requirement, in which the inputs are embedded costs. A transmission provider’s embedded costs include many items that themselves are not “transmission”: land, employees, computers, office buildings, the CEO’s desk, dues to professional organizations. If FERC (or a regional process) declared that a transmission-service provider must purchase a specified input to ensure that transmission service is reliable and based on reasonable cost, and if the transmission service at issue were regional transmission service whose costs are allocated regionally, then this input would have its costs allocated regionally. This category is close to, but not equivalent to, ancillary services; it consists not of items that are themselves transmission service but that are part of providing transmission service cost-effectively.

FERC regularly approves costs as prudent inputs to the revenue requirement for transmission or wholesale sales, but I am not aware of FERC’s ever ordering a utility to incur

⁷ S. Hempling, “Order 1000: Can We Make the Transmission Providers’ Obligations Effective and Enforceable?” Available at http://www.scotthemplinglaw.com/files/pdf/ppr_ntas-pprs_hempling0312.pdf

specific costs. (Rough analogy: A state commission might approve utility recovery of tree-trimming costs, and even penalize a utility for failing to trim trees, but it would be unusual for a commission to order a utility to incur specific tree-trimming costs. And if a commission did order a utility to trim trees, the state commission would not likely order a specific input cost such as a particular type of truck or chain saw. A line of cases protects the “management prerogative” from a regulator’s interference.) But FERC could achieve this result indirectly by declaring a rule of prudence (i.e., stating that a transmission provider’s failure to purchase a particular input service will result in higher costs than are necessary and that the utility risks disallowance of those higher costs).

V. Sponsorship: What are the rights for developers who “win” or “lose”?

A. The questions and the options

Order 1000 envisions competition among transmission providers for the right to have their projects included in the regional plan for purposes of regional cost allocation. Both incumbents and non-incumbents will spend money and time on studies and proposals. From these facts, several questions arise.

1. If a project is not selected in a particular process, can its sponsor try again in a later process?
2. Will all competitors be able to look at each other’s ideas, data, and studies?
3. If a project concept is selected, does its original sponsor have a legal right to develop it, or can anyone have a shot next at competing to develop and own the project?

I see no reason why a project cannot survive a loss and try again. A project concept does not lose its potential to benefit consumers just because it lost a particular competition. Load patterns could change, or the prior winner could leave the market before completing its own project.

As for access to data, the regional processes should develop procedures that preserve the competitive value of developers’ work; otherwise, developers will have less motivation to enter the market (that entry being a key purpose of Order 1000 and the ROFR-elimination rule). In the state-level competitive bidding process for generation, it is standard practice either to hire an independent entity to review the bids and recommend a winner to the commission, or for the commission itself to play that role, or to have the utility play that role (only if the utility is not a contestant).

Similarly, if the goal is attracting competitors, it does not make sense to invite ideas but then allow some competitors to use other competitors’ ideas.

B. Litigation: Should rejectees have a legal right to challenge their rejection?

The question is whether FERC can create a legal right in developers to contest what it considers unfair treatment.

Policy comment: The opportunity to litigate is a double-edged sword. On the one hand, the opportunity to challenge injects accountability. It mitigates incumbents' control and keeps information flowing about project benefits and costs. On the other hand, as long as litigation remains economical for the litigant (i.e., when the litigation cost is less than the probability of success times the profitability from success), the transmission-planning process will endure uncertainty, animosity, and inefficiency.

Legal comment: Whether a rejectee has a Federal Power Act right to challenge a decision links to a question addressed in the March NTA memorandum. The Act imposes obligations on FERC, as well as on public utilities that provide the service of transmitting electric energy in interstate commerce and selling electric energy at wholesale in interstate commerce. The obligation is to ensure that the terms and conditions of service are just and reasonable, and not unduly discriminatory. The beneficiaries of this obligation are the customers of the jurisdictional services, and the consumers served by those customers. As discussed in the NTA memo, nothing in the Act expresses any concern for sellers of inputs to transmission service or sellers of substitutes for transmission service—unless they are victims of undue discrimination because they are buyers of transmission service.

Based on this reasoning, FERC has no statutory obligation to create a legal path for rejectees to challenge their rejection merely because they lost a chance to develop a project. If an incumbent transmission provider self-interestedly and inefficiently rejects a non-incumbent's proposal, the statutorily relevant result is not the rejectee's lost opportunity. It is the (a) higher transmission costs for the region's customers, if the rejected proposal would have been lower in cost; and (b) higher wholesale power costs for the region's customers, if the rejected project would have allowed lower-cost power to displace higher-cost power. A subset of item (b) would be where the rejection causes one or more states to incur higher power costs to satisfy their renewable-portfolio statute.

This analysis means that FERC has no obligation to create a challenge path for proponents of rejected projects as victims of discrimination. The question is whether FERC even has the power to create a challenge path. The narrow answer is yes, provided the challenger is asserting the interests of customers, not its own interests. At least before FERC, it does not matter whether the person arguing the consumer interest is a consumer or a competitor, as long as the interest argued is the statutorily relevant interest. (Going to court is a different matter, because courts are Article III entities. To gain access to court, one must show statutory standing and constitutional standing. While a rejected supplier can show constitutional standing in the form of real economic damage due to the lost opportunity, the supplier could not show statutory standing unless it has an interest protected by the Federal Power Act (i.e., a consumer interest)).

There is a possible broader answer. It is possible that FERC could help create a developer's right to challenge, if FERC required utilities (including RTOs) to conduct the selection processes using independent entities, and required that the incumbents live with result (i.e., buy service from the selected entity). FERC could justify this order as necessary to ensure cost-reducing competition in the provision of transmission service. Having created an incumbent obligation to buy from a "winner," and having grounded that obligation in a Federal Power Act standard, FERC would have created a legal right in the developer. This is only a possibility; I am not aware of supporting case law.

In terms of creating a challenge path for developers of rejected substitute projects, where does this reasoning leave us? Here are some options and evaluations:

1. *Asking five presidential appointees* to resolve every supplier dispute is impractical and invites delay-inducing trips to the Court of Appeals (which are inexpensive relative to project profits).

2. *Having FERC delegate* dispute resolution to its staff is a possibility but still invites dozens of challenges that would tie up senior FERC staff.

3. *Relying on the incumbent* as the final word has statutory grounding, because the incumbent remains accountable in FERC cost-recovery proceedings to demonstrate its prudence. The transmission provider has the obligation to plan and serve, subject to the just and reasonable standard. The practical problem is that rejectees will not trust the incumbent's objectivity; and the proceeding on cost recovery could occur many months after the rejection, making it impractical for the rejectee to wait for a positive answer. Further, the FERC decision on cost recovery would be just that—cost recovery; it would not include a directive to the incumbent utility to choose the rejectee's project. More directly: I question whether FERC has the authority to order a utility to buy a product from anyone. FERC's authority is confined to ensuring that rates, terms, and conditions are just and reasonable and not unduly discriminatory (Section 205), and prohibiting any "rule, regulation or practice, or contract affecting" a rate for transmission service, if such an item is "unjust, unreasonable, unduly discriminatory, or preferential" (Section 206(a)).

4. *Requiring each regional process to use an independent entity*, whose decisions on project selection would bind the region. (See my March NTA paper for a general discussion of the independent entity.) The developer of a project selected by the independent entity would then have the right to build, as well as the right to recover costs regionally. This last phrase means that all retail utilities in the region would have an obligation to bear the project's costs as allocated by FERC. It is not clear, however, that FERC can order an incumbent transmission owner and other load-serving entities to fund projects owned by others, when they do not have a contract obligating them to make payments. FERC has said so, in Order 1000 at para. 529:

"529. [T]he Commission's jurisdiction is clearly broad enough to allow it to ensure that all beneficiaries of services provided by specific transmission facilities bear the costs of those benefits regardless of their contractual relationship with the owner of those transmission facilities."

But many dispute this authority. If the purpose of the independent entity is to reduce legal challenges by rejected projects (or others aggrieved by the selection or the resulting cost allocation), the independent entity's decision has to bind the relevant parties; or it has to gain a rebuttable presumption of justness and reasonableness so that the burden of producing contrary evidence is on the objector. Either of these approaches will require either more FERC action or voluntary agreement by the incumbents.

Conclusions

The ROFR-elimination rule removes the incumbent's ability to discriminate overtly against those who propose projects, but it does not prescribe specific actions to ensure nondiscrimination against them. Enlarging this weakness is FERC's decision to assign the job of implementing Order 1000 (in terms of developing criteria for projects to avoid ROFR by achieving regional cost allocation), in non-RTO regions, to the entities most likely opposed to the rule: the incumbent transmission providers.

To prevent misuse of this discretion, participants must ask: With what acts of discretion could an incumbent discriminate? For example, transmission providers will determine the qualifications to propose a project, application contents, and application timelines; and they will evaluate proposals. The procedures for each of these steps must be free of bias that prevents the best projects from seeking and achieving selection. Order 1000's mandate that transmission providers "consult" with their stakeholders in the planning process, and the Commission's existing authority to disallow imprudent costs, are not by themselves sufficient protection against bias.

In an important respect, then, the ROFR-elimination rule is weaker than Order 888. In Order 888, all transmission owners had to file a tariff whose original terms were written by FERC. FERC, not the incumbents, poured the concrete. (Incumbents were allowed to propose changes to the Order 888 tariff, but only after the FERC-prescribed tariff was on file and available.) In the ROFR context, in contrast, FERC is allowing the incumbents to determine the process—to pour the concrete. (The incumbents have to "consult" with stakeholders," but the incumbents still control the process and write the documents.) Worse, once the incumbents file these procedures with FERC and FERC accepts them as lawful, under judicial precedent any later challenger has the burden of proving them unjust and unreasonable, and/or unduly preferential.

This paper has identified several possible actions, for states, FERC and the regional discussions, that together can ensure neutral processes. The Appendix collects and organizes these recommendations.

Appendix of Recommendations

A. Prerequisites for Neutral Regional Processes

1. In each region, the process should stimulate and evaluate alternative means of satisfying the region's needs cost-effectively. ***In RTO regions, the process should be conducted by the RTO or an independent entity. In non-RTO regions, the process should be conducted by an independent entity.*** This process will produce evidence that FERC and state regulators can use to assess the prudence of incumbents' local proposals.
2. The process should:
 - a. ***start by specifying the needs of each load-serving entity. That specification should come from the states, or from each state's load-serving entities acting subject to the state commission's orders.*** State commissions determine that mix of generation, transmission, distribution, conservation, storage, and other resources that best serves their citizens. States therefore need to restore, and modernize, utility-specific integrated resource-planning processes so as to produce a clear statement of those states' needs and preferences and thereby frame the regional discussions for their citizens. Once those state power-supply preferences (in terms of load levels and power-supply mixes over some time period) are clear, the regional process should produce a plan representing that mix of transmission and non-transmission projects that will most cost-effectively connect the most economic sources for the desired power mix with the specified loads.
 - b. ***require the utility to announce that it is considering a project, well before the time when groundbreaking must occur and before the utility has done major studies.*** (This requirement would not apply to truly local projects, i.e., projects so local that there could never be a regional substitute for them.)
 - c. ***invite proposals for alternatives***, assess their relative costs and benefits, and deliver a neutral opinion.
 - d. from these proposals, ***create alternative regional plans*** that take into account all of the following: (a) regional projects eligible for regional cost allocation, (b) incumbent local projects subject to the residual ROFR, and (c) non-incumbent regional projects that could substitute for incumbent-proposed local projects.
3. ***Information about whether a ROFR exists for a particular project should be available sufficiently early in the planning process so that non-incumbents who compete for a slot avoid the risk of disclosing their data and analyses only to have the incumbent use that information for its own project.*** More generally, the regional processes should develop procedures that preserve the competitive value of developers' work.

B. Consequences for Incumbents If the Regional Process is not Neutral

4. Where a neutral process has not taken place, the rate regulators (states for retail, FERC for unbundled transmission and wholesale) should select one of these options:
 - a. *Eliminate any existing presumption of prudence* for, or regulatory deference to, an incumbent's proposed project.
 - b. *Reject the proposal, then create an opportunity for non-incumbents to compete* to carry out the incumbent's proposal (subject to their paying the costs incurred by the incumbent to create the proposal).
 - c. *Allow the proposal, but assign financial consequences*, where permitted by law, such as (a) reduction in the utility's transmission return on equity; (b) direct financial penalty; (c) for FERC, revocation of the affiliate's authority to charge market-based rates; and (d) disallowance of project costs to the extent they exceed the cost of the most cost-effective alternative.

C. Elimination of Incumbent Advantages from State Law

5. For eminent-domain powers, site control, right-of-way control: *Incumbents must share their resources with, or exercise their state law powers on behalf of, the non-incumbent in whatever way is necessary to get the non-incumbent equivalent access to the state-law benefit.* These requirements should be conditions on the incumbent's retention of the remaining right of first refusal left intact by Order 1000. Then, given this incumbent obligation, the qualifications process should assume the non-incumbent to have site control.
6. If the utility has state-law power to use its eminent-domain authority to assist a non-incumbent project, and the non-incumbent project will reduce the incumbent's cost of serving its customers, *then the utility that fails to assist deserves a prudence disallowance, or at least a denial of the presumption of prudence*, meaning that it must show that its refusal to assist was prudent. In its orders accepting tariffs that retain the incumbent's discretion to refuse assistance, FERC should make clear that it is preserving its authority to disallow imprudent costs arising from these situations.
7. *The region should not include public-utility status as a criterion unless that status is germane to a project's merits and there is no other way to replicate those merits.*