

proposal, there would be no interest paid, and after five years no additional payment to the Interconnection Customer would be made. Western also recommends that the Commission adopt a method to recover the costs of the Network Upgrades from the benefitting entities. It believes that current transmission customers should be held harmless from the cost impact of Network Upgrades that is not mitigated by increased transmission usage and associated revenues.

690. The North Carolina Commission recommends that the Commission modify its proposed rule to explicitly adopt the "but for" pricing policy for interconnection and transmission service in those states that have not yet unbundled retail electric service or implemented retail competition.

691. Several commenters, including National Grid, propose that the pricing issue can be resolved by analogy to the process of cost allocation for public roads. According to this analogy, the Interconnection Customer will have virtually sole use of the leads to the substation, just like the homeowner has sole use of his or her driveway. Thus, the cost of Interconnection Facilities, which are for the sole use of the Interconnection Customer, should be the responsibility of the Interconnection Customer. Next, the substation facilities needed to connect the sole-use facilities of the Interconnection Customer to the general delivery system are shared-use facilities, much like a local street. National Grid states that the cost of such facilities could be allocated partially to load and partially to the new Interconnection Customer. It explains that Network Upgrades that are remote from the Generating Facility typically allow movement of aggregate generation to aggregate load. National Grid contends that the benefits and use of such Network Upgrades are spread much more broadly and, like the highway system, could be rolled in and allocated to aggregate load within the market, or throughout an RTO if one exists. Finally, it argues that it may be appropriate to maintain an incremental charge for market-to-market transactions, but only where Network Upgrades in one market are needed by another market.

692. Peabody asserts that the NOPR contains certain provisions that are unjust and unreasonable as applied to large-scale base-load generation projects, especially coal-based projects. It urges the Commission to modify its interconnection pricing policy in such cases to require the Transmission Provider to roll the costs of Network Upgrades into its transmission rate base

without requiring the Interconnection Customer to fund the costs in advance.

Commission Conclusion

693. For Transmission Providers that are not independent entities, the Commission will continue to apply its current interconnection pricing policy, with certain revisions that are discussed below.

694. The Commission recognizes that its policy of requiring refunds to be paid to an Interconnection Customer for the cost of Network Upgrades constructed on its behalf is a controversial one. However, the Commission instituted this policy to achieve a number of important goals. First, consistent with the Commission's long-held policy of prohibiting "and" pricing¹¹¹ for transmission service, the crediting policy ensures that the Interconnection Customer will not be charged twice for the use of the Transmission System. The Commission determined that it is appropriate for the Interconnection Customer to pay initially the full cost of Interconnection Facilities and Network Upgrades that would not be needed but for the interconnection, but once the Generating Facility commences operation and delivery service begins, it must receive transmission service credits for the cost of the Network Upgrades. This ensures that the Interconnection Customer will not ultimately have to pay both incremental costs and an average embedded cost rate for the use of the Transmission System. Second, the Commission's crediting policy helps to ensure that the Interconnection Customer's interconnection is treated comparably to the interconnections that a non-independent Transmission Provider completes for its own Generating Facilities. The Transmission Provider has traditionally rolled into its transmission rates the cost of Network Upgrades required for its own interconnections, and the Commission's crediting policy ensures that Network Upgrades constructed for others are treated the same way. Finally, the policy is intended to enhance competition in bulk power markets by promoting the construction of new generation, particularly in areas where entry barriers due to unduly discriminatory transmission practices may still be significant. The policy is therefore

¹¹¹ When a Transmission Provider must construct Network Upgrades to provide new or expanded transmission service, the Commission generally allows the Transmission Provider to charge the higher of the embedded costs of the Transmission System with expansion costs rolled in, or incremental expansion costs, but not the sum of the two. Hence, "and" pricing is not permitted.

consistent with the Commission's long-held view that competitive wholesale markets provide the best means by which to meet its statutory responsibility to assure adequate and reliable supplies of electric energy at just and reasonable prices.¹¹²

695. While the Commission still finds these to be appropriate goals for an interconnection pricing policy, the commenters that object to the Commission's crediting policy make a number of valid points. Most importantly, as many point out, providing transmission service credits to an Interconnection Customer for the cost of Network Upgrades that would not be needed but for the interconnection of the new Generating Facility mutes somewhat the Interconnection Customer's incentive to make an efficient siting decision that takes new transmission costs into account, and it provides the Interconnection Customer with what many view as an improper subsidy, particularly when the Interconnection Customer chooses to sell its output off-system. In this regard, the Commission believes that, under the right circumstances, a well-designed and independently administered participant funding policy for Network Upgrades offers the potential to provide more efficient price signals and a more equitable allocation of costs than the crediting approach. The Commission notes that the transmission pricing policies that the Commission has permitted for an RTO or ISO with locational pricing, in which the Interconnection Customer bears the cost of all facilities and upgrades that would not be needed but for the interconnection of the new Generating Facility and receives valuable transmission rights in return, are acceptable forms of participant funding.

696. However, the Commission remains concerned that, when the Transmission Provider is not

¹¹² The Commission's crediting policy has also withstood judicial review. In an opinion issued February 18, 2003, the DC Circuit Court of Appeals affirmed Commission orders requiring a Transmission Provider to provide credits to Interconnection Customers for the cost of short-circuit and stability Network Upgrades. *Entergy Services, Inc. v. FERC*, 319 F.3d 536 (DC Cir. 2003). The court stated that "[t]he Commission's rationale for crediting network upgrades, based on a less cramped view of what constitutes a 'benefit,' reflects its policy determination that a competitive transmission system, with barriers to entry removed or reduced, is in the public interest." *Id.* at 543-44. The court concluded that "the Commission has reasonably explained that its crediting pricing policy avoids both gold plating and less favorable price signals such that the enlarged transmission system, which it views as a public good, can function reliably and continue to expand." *Id.* at 544.