

February 6, 2023

SB 68 - Providing incumbent electric transmission owners a right of first refusal for the construction of certain electric transmission lines.

Oral In-Person  
Proponent

FROM:  
Tony Clark, Wilkinson Barker Knauer, LLP on behalf of ITC Great Plains (conferee)  
[tclark@wbklaw.com](mailto:tclark@wbklaw.com) (202) 383-3354 (contact)

TO:  
Senate Utilities Committee

**February 6, 2023**

**Proponent Testimony  
of**

**Tony Clark, Wilkinson Barker Knauer, LLP on behalf of ITC Great Plains**

Mr. Chairman and Committee Members, thank you for the opportunity to appear before you today. My name is Tony Clark, I am a senior advisor at the firm of Wilkinson Barker Knauer LLP, and I am testifying today on behalf of our client ITC Great Plains.

By way of background, prior to my current role, I held various positions in state and federal government for over 20 years. I am a former two-term state representative in my home state of North Dakota. Subsequent to my legislative service, I was a member of our Governor's Cabinet. From 2001 to 2012, I was a Commissioner of the North Dakota Public Service Commission, approximately half that time as Chairman. From 2012 through 2016, I was a Commissioner of the Federal Energy Regulatory Commission (FERC). I'm hopeful that my diverse experience in energy regulation, especially my long-time support of state prerogatives in energy policy, will be helpful as you consider this legislation.

The issue of state rights of first refusal (ROFR) is one I have studied and been involved with for some time. North Dakota is among those states that has adopted a ROFR, and my time at FERC coincided with many of the compliance filings related to a federal rule (Order 1000) that established a complicated new regulation for transmission procurement. I will discuss my observations drawing from my time as both a state and federal energy regulator, and will relay how it informs my perspective today and why I support legislation such as this.

At the outset, I will note that I suspect you will hear from opponents of this legislation that this is a matter of monopolies vs. free market competition. It is a bumper-sticker argument that I frequently hear by those who have opposed similar legislation elsewhere. But it is a slogan that does not hold up to scrutiny in the context of transmission. I, and I think most regulators, would be the first to acknowledge that regulation is a second-best option to functioning competition. In fact, if this were a debate between a workable competitive industry framework on one hand, and traditional regulation of a franchised monopoly on the other, this would not be much of a debate.

But here is the distinction. In the absence of a workable framework for competition, certain industries exhibit monopoly characteristics such that more traditional regulatory tools offer a better outcome for consumers. The electric transmission industry is one of those examples.

Think of it this way. Whether you pass this legislation or not, the result will be monopoly transmission providers operating in Kansas. If you pass this law, it simply means that the monopolies that will build the transmission will be the ones whose service is most directly integrated with those utilities that serve customers in Kansas, and over which the state has the most direct regulatory authority. When something happens on the electricity grid, these are the entities with a local presence and existing Kansas-based facilities. If something goes wrong with this most important critical infrastructure, you as elected officials know who to call and where to seek accountability. In the absence of a state ROFR, a different federally concocted framework is imposed, in which certain portions of the transmission monopoly are bid out through a procurement process which has not worked in practice, and which facilitates the entry of merchant developers whose regulatory responsibility to Kansas customers is far less defined.

Whether Kansas adopts a ROFR or whether it defaults to FERC rules that otherwise mandate a complex, litigious transmission procurement policy, no customer in Kansas, large or small, is going to get to shop for their transmission provider in the same way they would shop for cell phone carriers, clothing, groceries or most other consumer products. There is no retail choice in the wires portion of the electricity business anywhere in the nation – even in those states, like Texas, that fully enacted so-called retail electricity choice.

Rather, the debate before you is about how to best structure your regulatory policy regarding the transmission monopolies you will have regardless. At its heart, it is a debate about whether transmission should be regulated in the traditional way, and as it has for most of the history of the electricity industry, or whether Kansas should subject itself to a newer federal transmission procurement process that has proven itself in practice to be both unwieldy and not in consumers best interests.

In order to understand how we arrived at where we are at this point in the electricity business, a brief history is in order. Prior to the mid-1990's nearly, if not all, states regulated utilities the same way. All were organized around vertically integrated utility entities – providing bundled generation, transmission and distribution service to end use customers. Through a series of both state and federal actions, various portions of that structure evolved over time. Some states unbundled their utilities into different business – such as separating the wires and generation portions of the business. In some instances this was paired with allowing customers direct retail access to their choice of middlemen energy retailers. This regime was adopted in about a dozen states before debacles like the Enron scandals and Western energy crisis effectively halted the restructuring movement. At the same time FERC was reforming other regulations within its purview. Among these actions were Order 888, which provided non-discriminatory access to the transmission grid, and Order 2000, which established the basic structure for what has become the regional grid operators (Regional Transmission Organizations) such as the Southwest Power Pool (SPP) that operates here in Kansas. This is how we have ended up with a utility system in which some states, like Kansas, still have vertically integrated utilities operating within an RTO; other states have a similar structure, but outside of an RTO; and others yet operate like Texas and Illinois, where the utility industry is fully unbundled. Yet throughout this period, not unlike your

local water utility, the wires portion of the business has remained a regulated monopoly because of its unique characteristics.

In 2011, FERC embarked on a path which would, among a lot of other changes, attempt an innovation in the transmission portion of the electricity delivery system. This is what is known as Order 1000. In it, FERC eliminated what had been a federal right of first refusal for certain transmission projects that were selected by regional grid planners. Rather than simply have the existing providers whose systems were impacted build needed new transmission, FERC created a procurement process by which a portion of the regulated transmission monopoly would be bid out. The rules by how this happens vary from region to region, but FERC specifically recognized state ROFRs – understanding that many states, like Kansas, continue to maintain a vertically integrated utility structure.

While the theory behind what FERC was trying to accomplish is perhaps understandable – “let’s try to interject some competitive bidding into the transmission monopoly” – in practice it has been a failure that is resulting in negative customer outcomes where it has been tried. To be clear, as I will discuss momentarily, I believe customer groups and policymakers will find they are mistaken if they believe that rejecting a state ROFR law will equate to lower utility bill. In fact, if this legislation is not enacted, I believe needed transmission will take longer to build and may end up actually costing more for customers for states that are situated like Kansas.

The reason for this is in the flawed nature of the FERC Order 1000 transmission procurement process that takes place in the absence of a state ROFR. With a state ROFR in place, when the regional grid planner identifies a needed transmission project, it assigns the project to the transmission owning utility that serves that particular region. It is sited and constructed by the entity that already knows the service territory, understands where lines can realistically be built, and how landowners will want them completed. The competitive aspect of this process takes place in the solicitation of labor and materials, in which the utility draws on those vendors and firms that are in the business of getting infrastructure built. In general, this system leads to efficiency and better certainty regarding the costs and timelines needed to build critical infrastructure. The costs for the project are overseen by regulators, and when completed, will be placed into rates as determined by the appropriate regulatory agencies.

Lacking a state ROFR, the process is less straight-forward. Once the grid planner determines a project is necessary, it puts it out for bid in a solicitation process. Developers of all kinds can submit a bid to become a new transmission monopoly. Some of these bidders may have deep experience in the field of utility infrastructure finance, construction and operation, some less so. Some may have on the ground knowledge of site-specific factors, some may not. Nonetheless, cost is an important component of the winning bids in this process. The incentive baked into this process may be to submit unrealistically low bids. There may be various strategic rationales for doing this, but among them is that once a vendor wins the project, experience with Order 1000 has shown they have found ways to attempt to get around cost containment commitments. In other words, the game becomes: win the project based on a bid that may or may not be realistic – but once you’ve won the project – you seek to place into rates not only your bid, but also the cost overruns. It’s a lose-lose for the state and customers. Your state’s most critical infrastructure may become dependent on companies with limited nexus to the state, and the rates your

customers end up paying may be more than they would have been if you just stayed true to the traditional utility regulatory model.

Furthermore, in practice, the solicitation process has proven too often to be a bureaucratic, litigious, expensive, time-consuming slog. Not only is there a cost to bidders responding to the solicitation itself, but the grid planners incur costs managing the process. In the case of SPP, these are costs ultimately borne by the end-use customers here in Kansas and throughout the region. Unsuccessful bidders can, and do, challenge the outcome of the process leading to further delay. In the end, the few Order 1000 projects that have successfully run the gamut and been placed into service have too often proven to be some combination of delayed, overbudget, or in at least one case, not operating as anticipated. In the instance one is delivered on-time and with some degree of budgetary success, policymakers would be right to conclude, as an old saying goes, “the game isn’t worth the candle.”

For a deep-dive on the perils of and poor outcomes delivered by the Order 1000 procurement process, I would direct your attention to excellent reports authored by the consultancy group Concentric. I have found these reports particularly persuasive because Concentric tracked the actual outcomes associated with Order 1000. This differs from other reports that attempted to quantify theoretical outcomes associated these projects, but with insufficient attention to how the whole regime was working in practice.

As noted by the 2019 Concentric paper, the average Order 1000 solicitation process to that point had taken over 500 days just to move from solicitation to selection. Some took well over 1000 days. The RTOs themselves spent millions administering the processes. And that is just the selection process. Actual permitting, construction and placing projects in service can add years more.

Concentric highlights several case studies arising from the Order 1000 solicitation process. In the interest of brevity, I won’t detail all of them, but I will review at least one in some detail to give you a flavor of the challenges.

One instructive example of these shortcomings is the project known as “Artificial Island” in New Jersey and Delaware. It was first identified by the RTO as early as 2012-2013 in an area that was identified as needing a transmission solution. PJM solicited more than two dozen ideas for alleviating the concern. By 2014 it had changed the technical specs for the project. Later in 2014, RTO staff recommended accepting a solution by one company, which was subsequently challenged by another company. The RTO board delayed selection throughout 2014 – including requesting assistance from FERC’s alternative dispute resolution service. By 2015, the RTO Board selected a different project. By 2016, that project costs had ballooned. This caused the RTO to go back and re-scope the project. Simultaneously, because the State of Delaware was so displeased with how my former agency proposed to allocate the costs of the project – the legislature got involved – attempting to block the construction of it unless the costs were instead allocated more heavily to New Jersey. New Jersey interests, not surprisingly, objected. The cost allocation litigation took several years to be considered by the courts.

This project, which consisted of about 3 to 5 miles of transmission line and facilities at each end of it in New Jersey in Delaware, has now, finally, after years of delay, been placed into service –

though at a cost that allowed for a \$20 million escalation over the original cost cap estimate. One can only wonder how many millions more were spent in regulatory and appellate litigation. Perhaps just as problematically, Concentric reported in a 2022 follow-up paper, that the project has had several subsequent performance challenges and was scheduled to undergo repairs late last year. One of the utility executives involved with this project said in Congressional testimony in 2018 that the “promised efficiency looks more like confusion, controversy and chaos.”

This is but one case study out of several outlined by Concentric, but the trend seems discernable. The Order 1000 process is broken. FERC itself also seems to recognize something is amiss. In a recent Notice of Proposed Rulemaking, it sought comment on reforming the rules that govern federal rights of first refusal, including putting on the table a proposal to allow for a reinstatement of a limited federal ROFR under certain conditions. It is yet to be seen whether FERC will adopt the proposal. It has generated significant discussion in filings, but regardless of the outcome of that rulemaking, there is widespread consensus that something is amiss with Order 1000, because projects either aren’t getting built as anticipated, or when they are, there are too often delays and cost surprises.

As a recovering regulator, for me, a particularly interesting question arises from this experience. “Why isn’t the solicitation process driving better consumer outcomes?” One persuasive theory is offered to FERC in a filing from PhD Economist Carl Peterson. Among his theses, which include the notion that Order 1000 merely “bids the monopoly” as opposed to offering true competition, is the nature of the information competing utilities have prior to submitting their bids. The grid planners will bid out projects under Order 1000, but at the time they do, in the case of a new transmission line, there is not necessarily a defined transmission route and specifications for exactly how the line will be constructed. Essentially, bidders may lack sufficient information to make a more accurate cost-based bid. Instead, the incentive is to just win the bid, and find way to place additional costs into rates later. The local utility that already serves an area is likely to have superior information about how transmission will need to be constructed in that state to gain approval, and regionally specific knowledge like the pool of available construction talent. The local utility will have a better sense for the type of pole configuration that landowners prefer and will be needed to gain local and state certificate approval in that geography and climate. The local utility also has better access to information about unique avoidance areas such as “no-go” zones regarding locally impactful cultural, historic and environmental factors. This means the local utilities’ bids are more likely to produce an accurate representation of total costs. A new entrant bids on the basis of a far less informed dataset. It seems like a plausible explanation of why there has been a recurring issue of Order 1000 selected projects seeking ultimate rate recovery in excess of the original estimates.

In closing, there are good reasons a growing number of states have already adopted ROFRs – especially here in the Midwest, where utilities are still overwhelmingly vertically integrated, state regulated entities. State leaders have come to understand that the results of the Order 1000 process are not meeting the promises made in support of it. From heavily Republican, “pro-competition” states like Texas, to deep-blue Minnesota, they see the consumer benefit and accountability that comes with a straight-forward regulatory structure that tends to get needed transmission built on-time and on-budget.

Thank you for your time today. I would be happy to answer any questions you may have.