November 30, 2012

Penny S. Murrell, Director
Division of Electric Power
Regulation - Central
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, DC 20426

Re: Southwest Power Pool, Inc., Docket No. ER12-2525-000

Dear Ms. Murrell:

This letter responds to your October 31, 2012 request for additional information concerning SPP's proposed Tariff modifications to revise Schedule 11 Rates for Through-and-Out Transmission Service. SPP's answers to those questions are provided below. Please let us know if you have any further questions.

1) In light of SPP's previous justification for zonal rates, please explain why through-and-out customers should pay a regional average rate reflecting the costs of facilities included in all the Schedule 11 zonal rates, instead of the zonal rate of the least-cost interconnected zone.

SPP transmission customers utilizing Point-to-Point Transmission Service to deliver power to load that exit outside the SPP region ("through-and-out") should pay a regional average of Schedule 11 zonal rates to eliminate inequities that exist as a result of the current rate structure that calculates through-and-out rates using the zonal rate of the least-cost interconnected zone. Additionally, a zonal rate based on a regional average will mitigate anomalies that occur in through-and-out zonal pricing resultant from the recently Commission-approved Balanced Portfolio transfers.

Pricing for through-and-out rates originally included in the Tariff were based on the average of all zones. The Tariff was changed in 1999 in order to facilitate more transmission business through SPP. The original implementation affected only Schedule 7 and 8 rates as this decision pre-dated Schedule 11 by several years. When Schedule 11 was later created in order to establish Base Plan funding, the same practice of using the lowest interconnected zonal rate was adopted for Schedule 11, even though the same rationale did not necessarily apply at that time. Additionally, the determinations of the lowest Schedule 7 and 8 rates and the lowest Schedule 11 zonal rate are independently calculated. Therefore, when the rates are combined to produce the rate for through-and-out transactions the result is a rate which is lower than the applicable Tariff charge for transactions sinking in either of the two interconnected zones.

Notwithstanding SPP's previous justification for a least cost zonal rate, SPP and the SPP stakeholders have recognized that the current rate methodology for through-and-out transactions results in inequitable treatment of customers in two ways: 1) Substantial variability among the Schedule 11 zonal rates for through-and-out transmission customers; and 2) transmission customers with load inside SPP may pay a substantially higher rate than through-and-out customers. The proposed Tariff changes are designed to mitigate or eliminate both of these problems.

Because through-and-out customers pay the least cost interconnected zonal pricing, the rate design results in load with a point of delivery ("POD") inside the SPP region, in many cases, paying a higher average rate than load with a POD outside the SPP region, even though they may both use the same facilities. The proposed changes in this filing better align pricing with the cost causers and appropriate zonal costs such that one class of customer is not paying a disparate amount. Commission approval of the Tariff changes in this docket will avoid this pricing disparity and provide more consistent treatment of transmission service exiting the SPP region. For example, through-and out service that sinks outside SPP pays a zero Schedule 11 zonal rate if the Point of Delivery external to SPP has any interconnection with the facilities of the Southwest Power Administration ("SPA"), a federal power marketing agency. SPA does not participate in building Base Plan upgrades; thus, there is no applicable Schedule 11 zonal rate for the SPA zone. As there is no applicable Schedule 11 zonal rate, through-and-out transactions that exits the SPP region and sinks in a zone that interconnects with SPA would have a Schedule 11 zonal charge of zero ($0.00). Conversely, transmission customers with load sinking within SPP (excluding SPA) would pay a Schedule 11 zonal charge. The Tariff revisions proposed herein intends to rectify this disparate result.

Another key consideration is that Schedule 11 zonal rates will be affected by the implementation of the "transfer" of revenue requirements from Schedule 11 zonal to Schedule 11 regional related to the Balanced Portfolio projects. Under the Balanced Portfolio cost allocation methodology, zonal revenue requirements associated with Schedule 11 are reallocated to regional cost recovery to ensure a benefit- cost ratio of 1.0 for the zones that otherwise would have a benefit-cost ratio of less than 1.0 as a result of the portfolio. The Balanced Portfolio's reallocation of revenue requirements ("Balanced Portfolio transfers") produces equity amongst SPP zones for the costs to construct upgrades which will benefit the SPP region. Consequently, this methodology results in even more disparity among zonal rates because certain zonal rates are further reduced, with some reduced to zero. By design, the Balanced Portfolio transfers move costs from zonal recovery to regional recovery. However, the Balanced Portfolio is not constructed with consideration of benefit-cost ratios for loads outside the SPP region. No analysis is conducted with regard to such loads and none is required under the Tariff. The balance of the portfolio is focused only on customer loads within the SPP region. For this reason, the rate structure applicable to external loads should be relatively neutral with respect to the balancing transfers. This is exactly the result that is achieved under SPP's proposal to utilize the regional average zonal rate under Schedule 11 for through-and-out service. By using the average, the differential effect of the zonal transfers is neutralized with respect to Schedule 11. With the Balanced Portfolio reallocations beginning in October 2012, this is an appropriate time to restructure the through-and-out rates in this manner.

With the Tariff revisions in this docket, SPP proposes that the region wide average Schedule 11 zonal charge be applied consistently to all transmission service that sinks outside the SPP region. Since through-and-out service does not sink within a SPP zone, the appropriate zonal rate would be an average of the zonal charges. This would ensure that through-and-out transmission service pays the costs associated the zonal portion of base plan funded projects. In other words, calculating transmission charges for through-and-out service using the least-cost interconnected zonal pricing has resulted in inequitable pricing among similarly situated SPP's customers. Therefore, SPP proposes to utilize a region wide average zonal rate for Schedule 11's charges. As the through-and-out transactions are not associated with any specific SPP zone, utilizing a region wide average zonal rate most fairly and equitable recovers the zonal costs when service sinks outside the SPP region. The result is a fair and non-discriminatory rate for transmission service that passes through SPP and exits the SPP region. Through-and-out customers will pay a region-wide average, zonal rate. The Tariff revisions filed in this proceeding put similarly situated customers (i.e., customers utilizing through-and-out point-to-point service that exits the SPP region) in the same rate structure regardless of which zone the transmission service is sourced.

As explained herein, the Tariff revisions in this proceeding were filed at the direction of SPP's Board of Directors and were thoroughly vetted by the SPP stakeholder process as a means to mitigate and/or eliminate the substantial variability and inequities existing in the current through-and-out rate methodology. Commission approval of the Tariff revisions will ensure that through-and-out rates are calculated in a fair and equitable manner; and are properly aligned with the Balanced Portfolio transfers recently approved by the Commission.

2) <u>Also, please explain how this proposal is consistent with the Highway/Byway rate design principles in general.</u>

SPP's Highway/Byway rate design was approved by the Commission in June of 2010 as a means to foster improvements in SPP's transmission system by consolidating and simplifying the cost allocation process.[1] With the proposed Tariff revisions in this docket, the Highway/Byway rate design principles remain intact and the proposed through-and-out rate is wholly consistent with the intents and purposes of the Highway/Byway cost allocation methodology. Consistent with the Highway/Byway rate design, the proposed through-and-out rates properly recover, at the level of an individual upgrade based on the nominal operating voltage, the costs associated with zonal usage. Put another way, the zonal rates are driven by the cost allocation of the individual upgrades as allocated by Highway/Byway rate design. The zonal allocation, based on nominal operating voltage, will be recovered throughout the footprint as determined on an individual upgrade level for the services traversing the zone.

As the Commission recognized in the Deficiency Letter, under SPP's existing Highway/Byway cost allocation methodology, SPP assesses zonal rates for all transactions sinking within SPP based on the cost of the facilities in the zone where the transaction sinks.[2] In fact, the Highway-Byway rate design was developed to determine pricing for transmission service for SPP load. Additionally, the Highway/Byway was developed as part of SPP's ongoing effort to move from a traditional transmission planning approach that focuses on local reliability issues to one that takes an approach to meet the needs of the region as a whole and which will facilitate integration of the western and eastern portions of the SPP region.[3] One such purpose was to allow renewable resources, located mainly in SPP's western footprint, to serve load in SPP's eastern footprint.[4] To the extent new facilities meet the needs of one of more zones their costs are allocated to the entire region.

The Highway/Byway methodology was developed with the assumption that Point-to-Point transactions sinking within SPP would be assessed the zonal component of the zone where the transaction sinks. Through-and-out transactions, by definition, service load outside the SPP and thus represent a different type of transmission service than what was contemplated when the

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[1] *See Sw. Power Pool, Inc*., 131 FERC ¶ 61,252 ("Order") (2010) at P. 4.

[2] *See Deficiency Letter*, Docket No. ER12-2525-000 ("Deficiency Letter") (October 31, 2012) at 2.

[3] *See* Order at 3-4.

[4] *Id*. at 3.

Base Plan funded rate design was implemented. The through-and-out rates are a "proxy equivalent" for the license plate rates being used in the SPP. The current tariff results in unjust and unreasonable rates since it always sets the rates at the "lowest" of the Schedule 7 or 8 rates, plus the lowest of the Schedule 11 zonal rates resulting in several exit rates having a combined rate lower than for customers which have load inside the SPP. This unintended consequence was not fully realized until enough Base Plan funded projects (Including Highway/Byway), were built that some of the border zones were not receiving zonal base plan funding which resulted in unjustly low exit rates.

As stated in the transmittal letter accompanying the filing, determining through-and-out rates utilizing the lowest interconnected Schedule 11 zonal rate has resulted in substantial variability in rates for transmission paths exiting the SPP footprint and is not consistent with the purposes of the cost allocation mechanisms developed for the Highway/Byway planning process. In other words, calculating transmission charges for through-and-out service using the least-cost interconnected zonal pricing has resulted in inequitable pricing which compromises the Highway/Byway methodology. The Tariff revisions submitted in this docket will bring through-and-out rates more in alignment with charges allocated to internal SPP transmission service.

3) <u>In light of the zonal rates applicable to the transactions sinking within SPP, please explain how the proposal to use an average rate reflecting the costs of facilities included in all of the Schedule 11 zonal rates for through-and-out customers is not unduly discriminatory.</u>

As previously discussed, this Tariff revision mitigates the comparability issues caused by entities which do not have a Schedule 11 base plan zonal rate, such as the facilities of federal power marketing agencies (e.g., SPA). Under the current rate design, these entities' participation in the Regional Transmission Organization ("RTO") give undue preference or advantage to those through-and-out customers which may not be required to pay a zonal charge based upon the zonal path of the through-and-out transaction.

The "unduly discriminatory" legal standard is a construct of statute.[5] The Commission has determined "that discrimination is undue when there is a difference in rates or services among similarly situated customers that is not justified by some legitimate factor."[6] As stated previously in this answer, determining through-and-out rates utilizing the lowest interconnected Schedule 11 zonal rate has resulted in substantial variability in rates amongst SPP's zonal areas and inequitable pricing for transactions exiting SPP's footprint. Under this methodology, transmission customers serving load that sinks within SPP may pay a substantially higher rate than through-and-out customers, which only utilize SPP transmission service to deliver load external to SPP; and therefore, through-and-out transactions may receive undue preference in pricing as compared to other transmission customers serving load internal to SPP. For example, the present least cost pricing is inequitable because a through-and-out customer pays, on average, a lower Schedule 11 zonal rate per KW than a typical transmission customer in the footprint. This anomaly is especially problematic in zones where the Transmission Owner does not have a base plan zonal rate under the Highway/Byway methodology, which allows a through-and-out customer to pay a $0 (zero) Schedule 11 zonal rate as the least interconnected cost rate.

Moreover, SPP is not unique in its rate design approach. Similar flat rate designs for PTP service sinking at the border or outside the footprint are included in the respective Tariffs of the

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5 For example, section 205 of the FPA states:

> "[n]o 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."

See 16 U.S.C. § 824d(b) (emphasis added). And section 206 of the FPA states:

> "[w]henever the Commission, after a hearing held upon its own motion or upon complaint, shall find that any rate, charges, 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."

6 *See, e.g., Sw. Power Pool, Inc.*, 137 FERC ¶ 61,075, at P 52 (2011); *Cal. Indep. Sys. Operator Corp.*, 132 FERC ¶ 61,148, at P 40 (2010). See also *W. Grid Dev. LLC*, 133 FERC ¶ 61,029, at P 17 (2010) ("The protection against undue discrimination prohibits the dissimilar treatment of similarly situated entities").

Midwest Independent System Operator, Inc. ("MISO") and PJM Interconnection LLC ("PJM").[7] As SPP's proposed Tariff revisions mitigate inequities seen in the current rate structure and produce a more just and reasonable rate methodology for all SPP customers, the Commission should find that SPP's proposed Tariff modifications are not unduly discriminatory and approve as respectfully requested by SPP.

4) <u>Please explain why consistent treatment of service is necessary under Schedule 11 but not under Schedule 7, which retains a zonal rate design.</u>

Schedule 11 rates are determined by SPP's planning and study process whereas Schedule 7 and 8 rates are developed primarily using the Transmission Owner's legacy planning costs prior to 2005 and localized planning information. As such, there is more relative variability in the Schedule 11 zonal rates. In recognition of the disparity between through-and-out transactions and transactions for load sinking within SPP, the SPP stakeholders decided to try move toward more comparable rate levels by bringing the exit rates closer to the rates paid by internal customers.

With the start of the phased implementation of the Balanced Portfolio reallocations, which was approved by the Commission effective October 1, 2012[8], the Schedule 11 point-to-point rates will be impacted much more significantly than the rates under Schedules 7 and 8. This is because the Balanced Portfolio reallocations are taken first from the Schedule 11 zonal revenue requirements. As explained in the response to the first question above, the Balanced Portfolio reallocations should have a relatively neutral impact on customers outside the SPP region that receive through-and-out service from SPP. However, this neutral effect does not occur with the current tariff provision of utilizing the least-cost zonal rate for Schedule 11. By modifying the zonal pricing component of Schedule 11 rates to utilize a regional average of the zones rather than a least-cost zonal approach, the SPP proposal would move the rate structure toward an appropriately neutral impact of the Balanced Portfolio reallocations on load external to the region.

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[7] *See* MISO Tariff, Schedule 7 (2) ("[Transmission Customer] shall pay the applicable single system-wide rate for (1) Firm Point-to-Point Transmission Service where the generation source is located within the Transmission System Region and the load is located outside of the Transmission System Region; and (2) Firm Point-to-Point Transmission Service where both the generation source and the load are located outside of the Transmission System Region); *See also* PJM Tariff, Schedule 7 and 8 (Providing a flat rate, in addition to other applicable charges, for PTP transmission service where the POD is at the "Border of PJM").

[8] *Sw. Power Pool, Inc.*, 141 FERC 61,149 (2012)

SPP stakeholders looked at different alternatives to bring equity to the discrepancy between through-and-out rates and internal rates. One alternative was to calculate exit rates based on the average of the Schedule 7 (or 8), and Schedule 11 zonal rates of all the interconnected zones. However, the stakeholders decided not to do this since it would very significantly raise the exit rates. Ultimately, the SPP stakeholder process decided to maintain the current lowest cost Schedule 7 or 8 rates and adjust the Schedule 11 zonal rate to the regional average. The result is a rate change for through-and-out transactions, but the new methodology solved the various issues related to the Schedule 11 zonal rates which have been previously pointed out in the transmittal letter and this response to the Deficiency Letter.

Respectfully submitted,
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