

1 **Q: Please explain FERC's "higher of" policy which prohibits "and" pricing and how**
2 **this is applied in a competitive jurisdiction such as PJM with transmission rights.**
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4 A. We understand the term “competitive jurisdiction such as PJM with transmission rights”
5 in this context to mean areas of the United States with an organized wholesale
6 competitive market operated by an Independent System Operator (“ISO”) that results in
7 locational marginal pricing (“LMPs”) – such as areas served by ISO New England, PJM,
8 New York ISO, Electric Reliability Council of Texas, MidContinent ISO, Southwest
9 Power Pool, and California ISO. LMPs reflect the marginal costs of energy and consist
10 of three components: variable energy costs, energy losses, and transmission congestion.
11 LMPs do not reflect the embedded costs of the transmission network. The embedded
12 costs are recovered through transmission rates paid by customers of the ISO. These
13 transmission rates are in addition to the LMPs and other charges.
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15 With this background, FERC’s “higher of” policy which prohibits “and” pricing works
16 relatively the same whether applied to transmission assets in a competitive jurisdiction
17 like PJM or applied to a non-competitive jurisdiction like in the southeast United States.
18 Specifically, in the PJM jurisdiction, for example, the amount of the transmission
19 revenue requirement will reflect the end result of application of the “higher of” policy
20 which prohibits “and” pricing. While every jurisdiction is different and the
21 implementation of the policy may result in differences in outcome, these are not due to
22 differences in fundamental policy. That is, the “higher of” and “and” pricing policy is
23 perfectly applicable in a competitive jurisdiction as it is in a non-competitive
24 jurisdiction.
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26 As an example of how the implementation of the policy may vary depending on
27 competitive vs. non-competitive jurisdiction, please refer to pages 19-21 of *Review of*
28 *Existing and Proposed Network Additions Policies for Newfoundland and Labrador*
29 *Hydro* for a description of FERC’s “higher of” policy and its relationship to “and”
30 pricing with respect to generation interconnection. As described in this section,
31 customers finance the transmission investment and are subsequently reimbursed. In
32 PJM, reimbursement may be either cash or through alternative mechanisms related to
33 transmission revenue rights, whereas this would not be the case in non-competitive
34 jurisdictions that do not have a financial transmission rights market. As mentioned
35 above, in these areas, transmission revenue requirements are recovered through
36 transmission rates outside of the competitive energy markets.