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August 1, 2011

**VIA HAND-DELIVERY**

Honorable Kimberly D. Bose, Secretary  
Federal Energy Regulatory Commission  
888 First Street, N.E.  
Washington, D.C. 20246

**Re: Filing of Midwest Independent Transmission System Operator, Inc.  
Regarding Annual CONE Recalculation  
FERC Docket Nos. ER11-\_\_\_\_-000**

Dear Secretary Bose:

Pursuant to Section 205 of the Federal Power Act ("FPA"), 16 U.S.C. § 824d, Part 35 of the Federal Energy Regulatory Commission's ("FERC" or "Commission") regulations, 18 C.F.R. § 35, *et. seq.*, and in compliance with Section 69.3.8 of the Midwest Independent Transmission System Operator, Inc.'s ("MISO") Open Access Transmission, Energy and Operating Reserves Markets Tariff ("Tariff"), MISO and the Independent Market Monitor for the MISO ("IMM") respectfully file the third annual recalculation of the Cost of New Entry value ("CONE")<sup>1</sup> for the MISO Region.

**I. BACKGROUND**

On March 26, 2008, the Commission conditionally accepted Phase II of MISO's permanent Resource Adequacy Requirements ("RAR") program, subject to completion of Financial Settlement provisions, and ordered compliance filings. MISO made a Financial Settlement compliance filing on June 25, 2008 which proposed, in part, to assess a Financial Settlement Charge on any Load Serving Entity ("LSE") that is deficient in meeting its RAR obligations (*i.e.*, an LSE that had not met its RAR obligations either through bilateral contracting or by acquiring Capacity in MISO's voluntary capacity auction). The Financial Settlement Charge is based, in part, upon the annual cost of new entry to develop a Capacity Resource in the Transmission Provider Region, which is determined by analyzing

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<sup>1</sup> Capitalized terms not otherwise defined herein have the meanings ascribed thereto in Section 1 of the Tariff.

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the capital, operating, and other costs that would be incurred for such facility. MISO established an initial CONE value of \$80,000/MW-month, which would be used in Section 69.3.7 of the Tariff to establish the Financial Settlement Charge for each month that an LSE is deficient.<sup>2</sup>

On October 20, 2008, the Commission conditionally approved MISO's RAR Financial Settlement proposal, including Section 69.3.8, which requires MISO to annually recalculate the CONE value.<sup>3</sup> The Commission also ordered MISO to make a compliance filing providing additional information to enable the Commission to determine the reasonableness of the initial CONE.<sup>4</sup> On November 19, 2008, MISO made a compliance filing supporting the calculation of the initial CONE value and the Commission approved the initial CONE value of \$80,000/MW-month on April 16, 2009.<sup>5</sup>

Section 69.3.8.b of the Tariff requires that MISO (the "Transmission Provider") annually recalculate the CONE and it also specifies some of the factors that MISO must consider in such a determination, as follows:

The Transmission Provider shall arrange for the CONE to be calculated annually in concert with the IMM by August 1 beginning on August 1, 2009. The Transmission Provider and the IMM shall consider factors, including, but not limited to: (1) physical factors (such as, the type of Generation Resource that could reasonably be constructed to provide Planning Resources, costs associated with locating the Generation Resource within the Transmission Provider Region, the estimated costs of fuel for the Generation Resource); (2) financial factors (such as, the hypothetical debt/equity ratio for the Generation Resource, the cost of capital, a reasonable return on equity, applicable taxes, interest, insurance); and (3) other costs (such as, costs related to permitting, environmental compliance, operating and maintenance expenses). In calculating the CONE, the Transmission Provider and the IMM shall not consider the anticipated net revenue from the sale of Capacity, Energy or Ancillary Services.

Section 69.3.8.c of the Tariff provides that MISO will annually file the revised CONE value with the Commission, to become effective the following Planning Year.<sup>6</sup> On July 31, 2009, MISO filed the first annual CONE recalculation with the Commission.<sup>7</sup> MISO filed the

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<sup>2</sup> To date, only one LSE has been found to be deficient and was charged the Financial Settlement Charge for a single month.

<sup>3</sup> *Midwest Independent Transmission System Operator, Inc.*, 125 FERC ¶ 61,060, P75 (2008) ("Financial Settlement Order"); rehearing denied, *Midwest Independent Transmission System Operator, Inc.*, 127 FERC ¶ 61,054, P37 (2009) ("Financial Settlement Rehearing Order").

<sup>4</sup> Financial Settlement Order at P 74.

<sup>5</sup> Financial Settlement Rehearing Order at P 45.

<sup>6</sup> In accordance with Section 1.508 of the Tariff, Planning Years commence on June 1st of a calendar year and conclude on the following May 31st.

<sup>7</sup> The Commission accepted the updated CONE value on April 27, 2011. See, *Midwest Independent Transmission System Operator, Inc.*, 135 FERC ¶ 61,082 (2011).

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second annual CONE recalculation with FERC on August 2, 2010, in Docket No. ER10-2090. That filing is currently pending before the Commission.

## **II. CONE RECALCULATION PROCESS**

### **A. CONE Calculation Discussed with Stakeholders**

MISO addressed the requirement to update the CONE value with MISO's Supply Adequacy Working Group during recent meetings. MISO explained at these meetings that it would be coordinating its recalculation with the IMM. MISO will continue discussing CONE and its derivation in upcoming working group meetings.

### **B. Approach Followed by MISO**

The most recent estimate of CONE in the MISO Region is based, in part, upon consideration of the CONE calculation provided by the IMM in the 2010 State of the Market Report, which was presented to stakeholders in June 2011. In that Report, the IMM presented information regarding the annual costs associated with two types of Generation Resources: gas combined-cycle Generation Resources and gas combustion turbine Generation Resources. The IMM concluded that the Estimated Annual Cost of a new combustion turbine Generation Resource in the MISO Region was approximately \$95,690/MW-year.<sup>8</sup>

MISO also analyzed the appropriate CONE value based upon the costs associated with a conventional combustion gas turbine generation unit.<sup>9</sup> MISO independently analyzed the IMM's inputs and then used net present value analysis to determine an appropriate CONE value. MISO considered many factors in its annual recalculation of the CONE value, including the following: (1) the type of physical generation facilities and the applicable fixed operating and maintenance costs for such facilities; (2) applicable financial factors (such as overnight capital costs); (3) an appropriate debt to equity ratio, depreciation time frame and project life; (4) interest rates and escalation factors; (5) consideration of tax implications; and (6) a reasonable return on equity for the generation facility.

The analysis assumed capital costs of \$704 per kW and fixed operating and maintenance of \$12.72 per kw-year for a new 160 MW combustion turbine. These figures were based upon data supplied by the Energy Information Agency ("EIA") for 2009 dollars, with an implicit price deflator of 1.028 from the Bureau of Economic analysis in order to convert EIA cost data from

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<sup>8</sup> See David B. Patton, Ph.D., IMM for MISO, 2010 State of the Market Report, p.8 (June 2011) (available at: <https://www.midwestiso.org/Library/Repository/Report/IMM/2010%20State%20of%20the%20Market%20Presentation.pdf>).

<sup>9</sup> Combustion turbines have been used as the basis for determining the cost of new entry in other RTOs and ISOs. See *PJM Interconnection, L.L.C.*, 126 FERC ¶ 61,275, P 39 (2009); *New York Independent System Operator Inc.*, 123 FERC ¶ 61,206, P 24 (2008).

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2009 dollars into 2011 dollars. In order to produce the annualized CONE value from these cost numbers, MISO and the IMM assumed: a 50/50 debt to equity ratio; a 20-year project life and loan term; a 5.6 percent debt interest rate;<sup>10</sup> a 3 percent Operation and Maintenance escalation factor; a 2.5 percent GDP deflator; a 43 percent combined effective federal and state tax rate; property tax and insurance costs of 1.5 percent of the capital costs; a calculated weighted average cost of capital of 7.60 percent; and a 12 percent after tax internal rate of return on equity. These factors and assumptions are comparable to those used by other RTOs in the development of CONE estimates. MISO's analysis concurred with that of the IMM and MISO concluded that the estimated annual cost of a new combustion turbine Generation Resource in MISO region is now approximately \$95,690/MW-year.

MISO also considered including in its CONE analysis a "cost of carbon" factor to reflect legislative discussions that have occurred during the last year regarding establishment of either a carbon tax or development of a carbon cost under a "cap and trade" approach, in part, because this environmental component might impact the CONE calculation. MISO elected, however, to not include such an analysis for the CONE for the next Planning Year because: (1) no federal carbon legislation has been enacted; and (2) various carbon proposals that are being discussed in Congress contain widely differing potential estimates for the cost of carbon. If carbon legislation becomes effective before August 1, 2012, then MISO will consider whether to include such analysis in its next CONE calculations.

MISO believes that establishing the CONE value for the 2012/2013 Planning Year at \$95,000 per MW-month<sup>11</sup> is just and reasonable, in part, because MISO's market for Capacity requires that Capacity costs be recovered during a relatively short time period, often only one month during the Summer. Also, unlike other RTOs where the CONE value is charged to parties to represent the actual cost of Capacity, in MISO the CONE value does not set capacity prices; the CONE value just establishes the level of deficiency penalties that will be charged to any LSE that is Capacity deficient. Therefore, it is just and reasonable to use the annual CONE value of \$95,000 per MW-year as the appropriate monthly CONE value to encourage compliance with Module E requirements.

### **C. Result**

MISO and the IMM jointly propose that the CONE value for the next Planning Year (June 1, 2012 through May 31, 2013) should be set at \$95,000 per MW-month. Accordingly, MISO and the IMM respectfully request that Section 69.3.8.b of the Tariff state as follows: "The CONE value shall be set at \$95,000/MW-month for the Planning Year commencing on June 1, 2012."

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<sup>10</sup> This figure was developed based upon current information regarding interest rates on 20-year bonds.

<sup>11</sup> For administrative convenience, the Midwest ISO is proposing that the annual CONE calculation be rounded down from \$95,690 to \$95,000/MW-year.

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### **III. DOCUMENTS SUBMITTED WITH THIS FILING**

Pursuant to Section 35.13(b)(1) of the Commission's regulations, no additional documents are being submitted with this filing because MISO is not proposing any new modifications to its Tariff sheets.

### **IV. EFFECTIVE DATE**

MISO respectfully requests an effective date of June 1, 2012 for the subject compliance Tariff sheet, in accordance with Section 69.3.8.c of the Tariff. MISO requests waiver of any applicable provisions of the Commission's rules and regulations to effectuate such a date.

### **V. NOTICE AND SERVICE**

MISO has served a copy of this filing electronically, including attachments, upon all Tariff Customers under the MISO Tariff, MISO Members, Member representatives of Transmission Owners and Non-Transmission Owners, the MISO Advisory Committee participants, as well as, state commissions within the Region.

In addition, the filing has been posted electronically on MISO's website at <https://www.midwestiso.org/Library/FERCFilingsOrders/Pages/FERCFilings.aspx> for other interested parties in this matter.

### **VI. CONCLUSION**

For the foregoing reasons, MISO respectfully requests that the Commission find that MISO has complied with the requirements in Section 69.3.8 of the Tariff and approve a CONE value of \$95,000/MW-month for the Planning Year that will commence on June 1, 2012.

Respectfully submitted,

*/s/ Arthur W. Iler*

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*Independent Market Monitor for MISO*

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**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary in this proceeding.

Dated at Washington, DC, this 1<sup>st</sup> day of August, 2011.

/s/ Christi Larson  
Christi Larson

Document Content(s)

Final CONE Filing for 2012 2013 Planning Year.PDF.....1-7