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Inside the battle over who gets to build the grid of the future

Robert Zullo

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The U.S. Department of Energy issued a draft report in February that found a “pressing need” for new electric transmission infrastructure across the country to improve reliability, connect a rapidly growing number of solar, wind and battery storage projects, supply increasing electric demand and alleviate scattered pockets of consistently high prices across the country.

To meet the future envisioned by the federal infrastructure act and the Inflation Reduction Act, which both contain major provisions to boost clean energy, the country needs to increase its current transmission system by an eye-popping 57% by 2035, the report says. Princeton University’s Net-Zero America study estimates expanding transmission capacity by 60% by 2030 will cost \$330 billion and tripling it by 2050 will cost \$2.2 trillion.

But in some states, bills that have been pushed by utilities to give them exclusive or preferential treatment for building regional transmission lines, called “right-of-first-refusal” laws, mean customers might pay more than they should for all those wires and towers, critics say.

“What’s important to note is that the clean energy transition is going to require a significant amount of new transmission. Because of that, that’s why you have these protectionist battles going on across the country,” said Sharon Segner, senior vice president of transmission policy at LS Power, a company that owns about 680 miles of transmission lines and has been awarded more than \$4 billion worth of competitively bid transmission projects.

“The incumbent utilities are trying to obtain a monopoly for the clean energy transition.”

The Edison Electric Institute, which represents investor-owned electric utilities and has pushed the Federal Energy Regulatory Commission to grant utilities rights of first refusal

for regional transmission lines, did not respond to a request for comment on the rationale for right-of-first refusal laws. However, in statehouses across the country, proponents have argued that such laws actually benefit consumers because they remove the incentive to offer unrealistic lowball bids to win solicitations, avoid delays dealing with procurement, preserve state regulatory oversight and result in streamlined, more efficient projects because local utilities know their communities better.

But they also represent a potential windfall for utilities.

“The more capital they spend, the more profit they make under government-guaranteed rates of return,” said Josiah Neeley, a senior fellow at the R Street Institute, a right-leaning free market think tank, in testimony on a failed right-of-first refusal bill in Wisconsin last year. “Historically, the absence of transmission competition has resulted in a severe lack of economic discipline — leading to cost overruns, with captive consumers footing the bill.”

‘Crony capitalism’

Last month, after a lawsuit by LS Power and another company, the Iowa Supreme Court halted legislation from 2020 that gave a right of first refusal for transmission projects to utilities operating in Iowa. The court, which ruled based on the manner in which the bill was passed, not its substance, nevertheless called it “quintessentially crony capitalism” and “rent-seeking, protectionist legislation” that will “impose higher costs on Iowans.”

That ruling comes as the U.S. Supreme Court weighs whether to take up a case involving Texas’ even more extreme 2019 law, which says the ability to build, own and operate new transmission lines that connect directly to an existing utility facility “may be granted only to the owner of that existing facility.” The U.S. Court of Appeals for the 5th Circuit held in August that the Texas law may violate the Commerce Clause of the U.S. Constitution, reversing a lower court ruling that upheld the law. The 5th Circuit, calling the law a “ban on new entrants in a market” remanded the case to the district court to consider whether Texas regulators can show they have “no other means to advance a legitimate local purpose.”

Writing for the conservative Cato Institute, Vanderbilt University law professor Jim Rossi called right-of-first-refusal laws (ROFR) “constitutionally suspect” and noted that of more than \$10 billion in transmission projects recently approved by the Midcontinent Independent System Operator, which operates the electric grid in all or part of 15 states, more than 90% will be built by incumbent utilities rather than competitively bid.

“State transmission ROFR laws reflect bad policy choices that thwart reliability in competitive regional power supply markets and, at bottom, are harmful to customers,” Rossi wrote. “Transmission ROFRs pose a barrier to a coordinated approach

to grid expansion, making it more difficult to promote reliability and new technological approaches that enable the lowest-cost power supply options for customers.”

According to the National Conference of State Legislatures, Indiana, Michigan, Minnesota, Montana, North Dakota, Oklahoma and South Dakota have laws on the books that grant utilities right-of-first-refusal privileges to build local or regional transmission lines. Mississippi passed similar legislation this year. Bills to add new ROFR rights or expand existing ones have been introduced in Missouri, Montana, Wisconsin, Oklahoma, Kansas and Indiana.

“If you want to see more clean energy we need more transmission and you want to keep all the options on the table for who’s going to develop those projects,” said Ari Peskoe, director of the Electricity Law Initiative at the Harvard Law School.

Current right-of-first-refusal laws at the state level have their origins in reaction to a FERC order in 2011 that sought to promote more competition in regional electric transmission projects in part by removing federal rights of first refusal for certain transmission projects.

“The agency reasoned that federal rights of first refusal might ‘be leading to rates . . . that are unjust and unreasonable,’ in large part because ‘it is not in the economic self-interest of incumbent[s] to permit new entrants to develop transmission facilities,’ even if those facilities ‘would result in a more efficient or cost-effective solution,’” the 5th Circuit judges wrote in their opinion.

Utilities, Peskoe said, “saw it coming and went to their legislatures and said ‘please protect us from this competition.’”

Just 3% of today’s projects are competitively bid, according to the Electricity Transmission Competition Coalition, which includes 70 companies and organizations from 48 states, including manufacturers, consumer advocates, transmission developers, retail electric customers and public power representatives.

Transmission tension

The legal battles over right-of-first refusal laws come as the Federal Energy Regulatory Commission grapples with a suite of issues surrounding transmission planning and construction, including whether to reinstate a federal right of first refusal for utilities, a move that is opposed by the U.S. Department of Justice and the Federal Trade Commission.

“American consumers and businesses should not be denied the benefits of competition when paying for this significant transmission investment,” the agencies said.

FERC, which regulates interstate electric transmission, is also exploring the concept of an independent transmission monitor. That's because some state regulators and consumer advocates say that as transmission spending by utilities is becoming an increasing portion of electric customers' bills, projects are escaping rigorous oversight because of varying regulatory regimes, a lack of expertise at the state level and too little transparency. FERC also has a draft rule out that would alter how regional transmission projects are planned and costs allocated.

And what's more, some critics argue, many utilities aren't incentivized to build the types of interregional transmission projects that the Department of Energy reported have the best benefits for customers.

The Texas case, they contend, is a textbook example of what's wrong with the status quo.

Building power plants, Peskoe said, has always been the major source of profit for utilities. New transmission lines that might bring in cheaper power from elsewhere reduce the need for those pricey new facilities.

"You're sort of cutting yourself off at the knees because you're reducing the opportunity to build power plants in the future," he said. "Bringing in energy from elsewhere may be good for the consumers but maybe bad for utility shareholders."

'They ran to their state legislature'

The Texas right-of-first-refusal law is being challenged by NextEra Energy Transmission, a subsidiary of utility giant NextEra Energy, which owns Florida Power & Light, the nation's largest utility.

NextEra had won a competitive bidding process in 2018 held by MISO to build, own and operate a 500-kilovolt line to be sited in a portion of east Texas covered by MISO but in Entergy Texas' service area. The estimated cost at the time was \$115 million. The next year, the Texas legislature passed the right of first refusal law, effectively allowing Entergy, which has three million electric customers in Arkansas, Louisiana, Mississippi and Texas, to take over construction of the line.

"The Texas utilities lost a legitimate competitive bidding process so they ran to their state legislature and passed a right of first refusal," said Segner, the LS Power executive.

Then, in 2020, Entergy issued a request for proposals for a 1,200-megawatt combined cycle gas power plant in the same "load pocket" (a term for a part of the electric grid where the transmission system doesn't have enough capacity to meet demand and requires local power generation) that would have been served by the transmission line. Entergy later decided it would "self build" the project, which is expected to cost about \$1.2 billion.

“If you don’t build transmission, you end up with load pockets. Entergy’s now using those load pockets to justify *billions* in gas unit installations instead of spending *millions* on transmission,” tweeted Simon Mahan, executive director of the Southern Renewable Energy Association, a nonprofit trade association that unsuccessfully urged FERC to deny MISO’s request to terminate the transmission line project.

SREA sees a disturbing trend, noting that a similar transmission project in Entergy’s Louisiana service territory, the Waterford-Churchill line, was also canceled after its cost-benefit analysis was “eradicated by local bottom-up transmission projects as well as the \$870 billion Entergy-built St. Charles (gas power plant).”

SREA said Entergy “appears to be using an anti-competitive strategy of capturing, delaying, and/or canceling transmission projects with local generation assets at significant cost to local ratepayers, while at the same time, not resolving underlying load pocket problems.”

Entergy rejects that argument.

The Orange County, Texas, plant “was needed to address a large and growing shortfall of generation for Entergy Texas,” said company spokeswoman Kendra James, adding that growing electric demand and the retirement of older power plants from the 1970s were also factors.

“The OCAPS plant will address issues that the Hartburg-Sabine Junction Project could not, even under the most favorable assumptions for that transmission line,” James said. “There is no reasonable argument that Hartburg-Sabine was a substitute for OCAPS.”

Entergy, James added, has more than doubled its capital investment in transmission since 2014 to improve reliability, connect new customers and reduce congestion on its system.

“To provide reliable and affordable electric service, public utilities such as Entergy must invest in electric generation, transmission, distribution, and other aspects of the utility’s business,” she said. “Every investment decision we make is based on what we think is in our customers’ best interests.”