

- 1) In paragraph 267, two alternate schemes for computing of the Losses component of the Transmission Usage Charge under the LMP system are discussed. One method computes the difference in the real-time marginal cost of losses at the points of delivery and receipt. All customers are assessed at the marginal rate, the rate associated with the addition of the next MW of load to the system. The second scheme proposed charges all customers at the average cost of losses. Although the Commission indicates a preference for the Marginal Losses approach, it seeks comment on the relative merits of each method.

The Commission correctly observes that the Marginal Loss approach will treat each increment of load as if it were the last MW added to the system. Due to the non-linear behavior of transmission losses with increasing load, applying this method to all transactions will lead to over collection of the revenue necessary to purchase the energy needed to supply total system losses. The accepted method for compensating for this over collection is to credit the overpayment against the uplift charges assessed each Load Serving Entity.

There are two primary advantages to the use of the Marginal Loss approach that we feel offset the issue of overpayment. First, the basic premise of LMP is to charge all users at the Marginal Cost of the next unit of Energy. This supplies a clear signal to the customers of the current cost of energy. Charging for losses at the margin is therefore consistent with this premise. It signals to the customer the current cost of losses specific to his transaction.

Second, the use of the Marginal Loss method also assesses each user of the transmission system according to his actual use of the facilities at the time he is using them. This means that someone scheduling a transaction through a heavily loaded interface in the direction of predominant flow is charged a rate proportional to the instantaneous conditions at the time of the last dispatch. Similarly, someone who has scheduled a counter-flow transaction that actually reduces total system losses is credited in proportion to that reduction rather than having to pay an average rate based upon everyone's use of the system. Each user pays (or is paid) according to his actual points of receipt and delivery and according to actual flow conditions at the time of the dispatch. We note that congestion charges are based on the difference in the marginal cost of energy at the points of receipt and delivery of the specific transaction, not on an average cost of congestion over the entire system. The marginal loss methodology is therefore perfectly consistent with the method by which congestion charges are determined.

In contrast, the Average Loss method blunts the economic signals generated by the instantaneous condition of the transmission system by computing an average loss factor for "typical conditions" and socializing that over all users of the

system. While the averaging method is simpler to apply and does not necessarily and fundamentally over collect, it is an imprecise and inelegant method in comparison to the Marginal Losses method and does not fairly distribute the cost of losses to those who are contributing most to them.

- 2) In paragraph 268, the Commission proposes to allow both financial and “in kind” payment for losses. While the concept of being able to pay for losses in kind by injecting more energy into the system than is ultimately withdrawn is appealing to suppliers who feel they perhaps have more control over their costs, the complexities introduced by this practice far outweigh any true advantages.

A financially based loss payment system is much simpler to schedule. The transaction is characterized by its face value amount in all communications that occur. For complex hubbed transactions or those that span more than one RTO, the additional data structures needed to track each payback increment and its ultimate destination make the physical payback method unwieldy at best. The LMP system, with its elimination of the need to obtain transmission reservations has the potential to greatly simplify the scheduling process. It would be a step backwards in this trend toward scheduling simplification to require accommodation of physical loss payback that is bundled with the original transaction.

For a physical loss payback system to work, it is necessary to determine in advance the loss amount so that it can be scheduled. This means that a loss percentage must be computed based upon average or typical conditions. The use of this average percentage blunts the economic signals sent by the transmission system regarding its use at the time of the transaction. It tends to socialize the cost of losses over all users of the transmission system. As pointed out in the discussion of paragraph 267, the computation of Marginal Losses at the time of dispatch assesses charges to the user that are specific to his points of delivery and receipt and to the actual conditions at the time of the transaction. These charges will be more for those who are contributing most to total system losses. It may actually be negative for those scheduling counterflow transactions.

From the viewpoint of the energy supplier, it would make more sense for him to bid the extra increment of “in kind” energy he would have used for physical payback into the real-time spot market as a price taker and receive payment for that energy at a rate equal to the LMP at his bus. This payment should offset the TUC losses charges he incurs.