

**Summary of Testimony of  
Nora Mead Brownell  
Commissioner, Federal Energy Regulatory Commission  
Before the Committee on Energy and Natural Resources  
United States Senate  
March 27, 2003**

I want to commend the Committee for pushing forward on the difficult issue of restructuring electricity markets. I believe that we are at a point where it is imperative for leadership to set the tone, the principles, and the framework for moving forward. We are at the point where, I believe, we need to make sound legislative and regulatory calls to restore confidence to customers and investors and bring the energy sector out of its battered and beleaguered state.

The legislative proposals address a wide range of electricity restructuring issues and contain numerous reforms to the current laws, many of which I believe will go a long way toward helping to create and sustain a healthy energy sector. I appreciate the willingness to think innovatively about regional approaches. The current federal and state regulatory framework did not envision regional markets so we must address roles and responsibilities. I do, however, have questions about the Regional Energy Service Commission proposal and would welcome the opportunity to work further with the Committee on thinking through the appropriate structures to address regional issues.

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**I. Background**

Thank you for inviting me and giving me the opportunity to share my views on the legislative proposals to restructure electricity markets. I want to commend the Committee for pushing forward on some very difficult issues. I believe that we are at a point where it is imperative for leadership to set the tone, the principles, and the framework for moving forward. We are at the point where, I believe, we need to make sound legislative and regulatory calls to restore confidence to customers and investors and to bring the energy sector out of its battered and beleaguered state. We are witnessing a silent and insidious deterioration of our infrastructure.

The legislative proposals address a wide range of electricity restructuring issues and contain numerous reforms to the current laws, many of which I believe will go a long way toward helping to create and sustain a healthy energy sector. There are a few areas, as described below, where I believe further evaluation and discussion is warranted.

**II. Pending Legislative Proposals on Electricity Regulation**

**A. Regional Energy Service Commissions**

As I understand it, Section 1211 of the Senate Staff Discussion Draft would authorize States to enter into agreements to establish Regional Energy Services Commissions (RESCs) that could then have jurisdiction over transmission planning and

siting, rate design and revenue requirements for transmission and wholesale sales, market power review and market monitoring, formation and approval of "Transmission Organizations," reliability standards and rules, and enforcement mechanisms. Public utilities in States in an RESC would not be subject to Commission authority under the Federal Power Act (FPA) Part II, except for section 204 and parts of 202 and 209.

As the Commission has stated on numerous occasions and as the Discussion Draft reflects, energy markets are regional in nature. For more than 10 years now, from Regional Transmission Groups in the early 1990s to recent proposals for Multi-State Entities, the Commission has supported and encouraged regional solutions to energy issues in the energy markets. Presently, I believe we have success stories where States have worked together on resources and planning. I also know that there are hurdles to overcome if we expect States by themselves to move beyond opening lines of communication to actual implementation of solutions for the more intractable regional problems. I believe that such difficult issues as infrastructure planning, identification of resource needs, market monitoring and independent operation of the grid are among those that should be considered on a regional basis. I also believe that regional transmission organizations (RTOs) that are independent from market participants both in perception and reality and are guided by a consistent set of regulatory principles are the best forum for addressing these issues. We have also emphasized the important role for states in leading these policy discussions through multi-state entities or some other structure.

While I share what I believe to be your vision for allowing state input and regional flexibility and variation, I am concerned that the proposal largely eliminates any consistency in regulation as currently afforded to the industry under the FPA. I would suggest that we study the following:

- Presently all utilities enjoy a common set of rules and requirements provided for by the FPA. The Draft permits the creation of governor-appointed regulatory commissions, each of which could have different due process requirements (or decide to have none at all); different filing requirements for rates, terms and conditions of service; different rate policies and incentives and terms and conditions for interconnection to and access to the transmission grid. What are the practical effects of introducing regional variation in areas that have already been standardized nationally?
- RESCs only need to seek to ensure no undue discrimination; there does not appear to be any requirement to ensure just and reasonable rates, terms and conditions of transmission or wholesale sales of energy. Would the RESCs be charged with ensuring just and reasonable rates or would FERC retain jurisdiction to do so? If the RESCs are given such jurisdiction, what if just and reasonable rates are defined differently in each region? What if undue discrimination is defined differently in each region?

- It appears that the public utilities and market participants would have no ability to seek review of any decisions - - either from the RESC or through appellate rights to the Commission or to a court. How will due process rights be protected?
- It is unclear from the Draft whether public utilities governed by RESCs would be exempt from the Commission's investigatory, enforcement, accounting and auditing requirements. Is that the Committee's intent? If not, will FERC have the information or tools necessary to perform these functions?
- Is it the responsibility of the appointees to be governed by state needs or regional needs?
- How does a multi-state utility whose territory covers multiple regions assure compliance to multiple sets of rules? How does it effectively participate in the stakeholder process? Will multiple rules require companies to restructure their companies by region? Will RESCs cause added personnel and regulatory and compliance costs? How will we measure the cost/benefit of the model? Could DOE provide a study? Could DOE provide an analysis of what regions should look like to maximize efficiency?

- The major criticism from investors, rating agencies, and bankers has been the lack of certainty caused by the failure to complete the restructuring started in 1992. Will the possibility of as many as 20 sets of regional rules on rates, terms and conditions of service, and cost recovery, among others, resolve those concerns?
- New technologies have been slow to be applied in this market place. Will regional variation on issues such as queuing, interconnection, transmission access, and technology application act as a barrier to entry? How will technology manufacturers adapt to variations? Will we lose manufacturing efficiencies?

I agree that the time has come for change. I believe that regional variation has been acknowledged and implemented in RTO dockets. Further, I believe that FERC has acknowledged the need for state involvement in regional planning, siting and market monitoring. But, we must look to solutions that create regulatory certainty and clarity and that reflect what we have already learned about the highly integrated and interdependent nature of this nation's energy markets.

## **B. Reliability Standards**

Each of the legislative proposals under consideration today provide for an electric reliability organization (ERO) to develop and enforce reliability standards applicable to all users, owners and operators of the bulk power system. The Commission would certify

an organization as an ERO and the Commission would approve the security and reliability standards and enforcement provisions of the ERO. All users, owners and operators of the bulk power system would be required to comply with the reliability standards. The approach envisioned by the legislative proposals is precisely what is needed in the evolving competitive electricity markets. What has been missing in the past and what this legislation adds for the future is accountability. Under existing law, there are no legally enforceable reliability standards. Compliance with the reliability rules established by the North American Electric Reliability Council (NERC) is voluntary. Therefore, it is difficult to assess (and impossible to ensure) whether the best job is being done by NERC and the market participants to preserve reliability.

**C. Open Access (FERC-Lite)**

Section 31 of the Senate Staff Discussion Draft and Section 7021 of the House Subcommittee version would grant the FERC the authority to require all transmitting utilities (not just those that constitute "public utilities" under the Federal Power Act) to offer open access transmission service, with some exceptions, *e.g.*, unless they sell no more than 4 million megawatt hours of electricity per year.

I support the intent of these provisions to ensure a properly functioning and transparent transmission grid. At the same time, I understand the concerns of parties not now subject to open access, and I believe that we must work to ensure that their rights are protected.

#### **D. Transmission Siting**

Studies report that the nation's infrastructure is lacking.

- Transmission investment is not meeting the growing peak demand - - the amount of new transmission added in the past 2 decades has consistently lagged behind growth in peak demand.
- NERC reports that investment in new transmission facilities is lagging far behind in new generation and growth in electricity demand. Construction of high voltage transmission facilities is expected to increase by only 6 percent (in line-miles) during the next 10 years, in contrast to the expected 20 percent increase in electricity demand and generation capacity. The cost of transmission accounts for less than 10 percent of the final delivered cost of electricity in what is today a \$224 billion industry.

Several of the bills under consideration address the siting problem. Section 1222 of the Senate Staff Discussion Draft would give the Commission siting authority for transmission facilities in "congestion zones" determined by the Department of Energy if a State fails to start action on an application within 60 days of its filing and finish within 18 months. However, the Commission would have no authority if the State has vested its siting authority in a Regional Energy Services Commission. As discussed above, I have several questions regarding the workability and implementation of RESCs. Section 210 of the Senate Counter-Offer would allow two or more States to enter into a compact for



regional transmission siting agencies. Section 7012 of the House Subcommittee bill includes many of these same points, but without the concept of a Regional Energy Services Commission.

I believe that state-by-state siting of such transmission superhighways is an anachronism that impedes transmission investment and slows transmission construction. We should not allow this relatively small cost to prevent consumers from enjoying reliable service and the low cost of alternative supplies. It is past time that someone address this elephant in the living room. I am not wedded to any particular legislative approach, but I do believe that some Congressional action on this issue is needed to help ensure that enough transmission is built to provide customers with reliable and reasonably priced electricity. This is an area where a regional perspective is needed.

**E. Transmission Investment Incentives**

Several of the legislative proposals would require the Commission to adopt rules on transmission pricing to encourage the economically efficient enlargement of transmission networks, the deployment of transmission technologies to increase capacity and efficiency, and the reduction of transmission congestion. I support these proposals and note that the Commission has already issued a "Proposed Pricing Policy for Efficient Operation and Expansion of Transmission Grid" that is consistent with the proposed legislation.

Some have expressed concern that incentives are extraordinary and unnecessary costs for consumers. They ignore three realities: transmission is 10% or less of the total bill, transmission enables access to lower cost generation which may well offset the costs of associated transmission, and the fragility of our nation's transmission system has serious security and economic repercussions which we cannot ignore.

**F. Transmission Cost Allocation (Participant Funding)**

Section 33 of the Senate Staff Discussion Draft would require the Commission to adopt rules on allocating the costs of “interconnect[ing] new transmission facilities as well as the modification, expansion or upgrade of existing transmission facilities....” The rules must ensure that all users of a transmission expansion “bear the appropriate share of its costs.” The cost of transmission expansions not providing “system-wide benefits” and instead primarily benefitting only a subset of users or market participants must be recovered from that subset incrementally. System-wide benefits would include providing reliability and adequacy for regional needs; accommodating load growth on a regional level; increasing transmission capability into congested areas; and facilitating major regional and inter-regional power transfers.

The House Subcommittee bill provides that “upon the request of a regional transmission organization or other Commission-approved transmission organization, new transmission facilities that increase the transfer capability of the transmission system shall

be participant funded.” The Commission would be required to “provide guidance as to what types of facilities may be participant funded.”

I believe that the Commission needs to address issues surrounding cost allocation of new interconnections and grid expansions. This country desperately needs a strong transmission grid, which in turn necessitates a cost allocation mechanism that gets infrastructure built and encourages innovation and new technology. I believe that an independent transmission organization can ensure nondiscriminatory access and rate treatment.

#### **G. Transmission Organizations/RTOs**

Section 212 of the Senate Counteroffer and section 7022 of the House Subcommittee bill state the sense of the Congress that "all transmitting utilities should voluntarily become members of independently administered regional transmission organizations [RTOs] that have operational control of interstate transmission facilities and do not own or control generation facilities used to supply electric energy for sale at wholesale."

I continue to believe that creation of RTOs is the single most effective way of achieving a vibrant, competitive electric market. RTOs that are fully independent of market participants can ensure non-discriminatory operation of the transmission facilities under their control. RTOs have FERC-approved market monitors, implement FERC-approved market mitigation plans, and conduct long-range planning all for the protection

of customers. RTOs can perform economic dispatch over large geographic areas that will ensure the selection of least-cost generators. Finally, RTOs can offer organized markets and one-stop shopping that reduce transaction costs, provide transparent market rules and allow the opportunity for price discovery.

Therefore, I strongly support Congressional encouragement of RTO formation.

#### **H. PUHCA**

I believe that these legislative proposals strike an appropriate balance by replacing PUHCA with increased access by the FERC and state regulators to certain books and records.

#### **I. PURPA**

I support the general approach to PURPA included in the draft bills. I support prospective elimination of the forced sale provision of PURPA provided that qualifying facilities have access to a competitive market and provided there are appropriate transitions rules to recognize the rights and obligations of parties.

#### **J. Market Transparency, Anti-Manipulation, Enforcement**

Some of the legislative proposals would require FERC to issue rules establishing an electronic information system, accessible by the public, specifying the availability and price of wholesale power and transmission services. While I support the goal of transparency in energy markets, I believe that there may be more efficient ways of

reaching that goal than having the government take over collecting and reporting information on prices.

The legislative proposals also would prohibit round trip trading and the filing of false information on wholesale power prices. Banning these practices will help ensure customers that power prices are not being manipulated.

The legislative proposals also would significantly increase the penalties available under the FPA. The FERC must have an expanded role in monitoring for, and mitigating, market power abuse. The enabling statutes of the Securities and Exchange Commission and the Federal Communications Commission provide for a range of enforcement measures, such as civil penalties. I believe that providing FERC with similar authority would send a powerful message to electricity market participants that we take violations of the Federal Power Act just as seriously.

#### **K. Consumer Protections**

I support allowing refunds from the date a complaint is filed, as opposed to 60 days after the filing. This proposed change will better protect customers. I also support the proposals to extend refund liability under FPA section 206 to large non-public utilities for spot market sales violating Commission rules.

#### **III. Conclusion**

Thank you again for the opportunity to offer my views on the legislative proposals to restructure electricity regulation pending before your Committee. While I have

discussed the approaches in the bills generally, I would be happy to provide technical comments in the future if it would be helpful to the Committee.