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Refunds, Other Penalties Justified By Anticompetitive Behavior, ELCON Says

If wholesale markets demonstrate anti-competitive behavior such as physical or economic withholding, the Federal Energy Regulatory Commission must act swiftly to impose remedies, including ordering refunds, ELCON said in comments to the Commission. FERC has an obligation to prevent obstacles to the development of the bulk power markets.

The comments came in response to a FERC staff conference this year on utility market-based rate authorizations. Last fall, FERC suspended the market-based rate authority of American Electric Power, Entergy and Southern during peak hours after each was found to exercise market power during these times. That rule was later stayed after an outpouring of protests

from the generator community and Wall Street. The Commission also proposed essentially to require refunds by utilities found to engage in anticompetitive behavior or to exercise market power.

In response to generator protests that suspending market-based rate authority could inhibit investment in utilities, ELCON said clearly articulated rules -- even involving potential penalties -- and quick, firm action by FERC would reduce regulatory and investment risks. Uncertainty is created when the rules (and

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Letter to FERC: You Have Duty to Require Refunds

ELCON and several ally organizations representing industry, public and rural power, and transmission-dependent utilities wrote the Federal Energy Regulatory Commission that FERC has a statutory duty to adopt its proposed Market Power Abuse Refund Obligation throughout the United States, applying it as necessary even in areas where regional transmission organizations

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FERC Chair Pat Wood Keynotes 2002 Seminar

The 2002 ELCON/PGC Seminar this Oct. 10-11 at the Crystal City Hyatt Regency, Arlington, Va., features Pat Wood, chairman of the Federal Energy Regulatory Commission, as morning keynote speaker, Thurs., Oct. 10. Other confirmed speakers are Friday keynoter Erroll Davis, CEO of Alliant Energy and new chairman of the Edison Electric Institute, and Thursday luncheon speaker David Svanda, member of the Michigan Public Service Commission and incoming chairman of the National Association of Regulatory Utility Commissioners.

This year's theme is "Coping with Uncertainty and Volatility: The Energy Manager's Dilemma." Register on-line at www.elcon.org or by calling ELCON's office.

Enron Tip of Iceberg, ELCON Tells FERC

ELCON urged the Federal Energy Regulatory Commission and Congress to look carefully at the facts emerging about Enron's activities, because they describe a real, ongoing problem with the electricity market.

"Recent revelations about Enron's efforts to manipulate the market in California and the West point out what many of us have been saying for a long time: any centrally administered bid-based market is simply too easy to game," said ELCON Executive Director John Anderson. "When a market structure allows an energy supplier to push prices up by withholding supply, the natural desire to maximize profits will be too great to overcome. Consumers big and small then get hit with a double whammy

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Mark Your Calendar! 2002 ELCON/PGC Seminar Oct. 10-11

Let's Not Dismiss the Benefits of Competition

Can you believe what is happening in electricity markets? The self-immolation of Enron, including a series of self-serving partnerships, auditors who didn't audit, and executives who exhibited egos that would make Sigmund Freud proud, was page one news for weeks. For a while it was somewhat entertaining (as long as you were not a former Enron employee).

But then charges got more serious. There were charges of market manipulation. The high prices in California and the West were not just the result of high demand and low supply as we had been told. Rather, there were allegations of

By Carol
Hyams
Guthrie,
ELCON
Chair

lessly about who did what to whom. We need to construct electricity markets that work, that provide proper incentives, and that deliver low-cost, efficiently produced, reliable power to all consumers, large and small.

That having been said, I am still a believer in the power of the market. And I still believe that, in almost every instance, competitive markets are better than monopoly markets.

At ELCON we began advocating more competitive electricity markets about 15 years ago. As energy managers for America's largest corporations we knew that monopoly utilities treated us as captive ratepayers, not as customers. Accordingly, we knew that monopoly utilities had absolutely no incentive to seek ways to provide lower cost electricity.

We believed then -- and we believe now -- that only through true competition, at the wholesale and retail level, can we ensure that our electricity system supplies power at the lowest cost to the consumer. Unfortunately, competition has taken a bit of a beating lately. That is because politicians and regulators tried to hard to ensure that "competition" was all things to all people, and they tried even harder to ensure that "competition" would never, ever, let prices go up - a noble but clearly doomed objective.

Quite simply, what happened in California was not competition. It was a political effort to restructure - and in many ways re-regulate - the electricity industry. And it was a dismal failure for a number of reasons. But that should not doom the fate of competition.

I have seen competition successfully replace regulation in other industries. Every time I want to travel, I can go on the web and easily compare routes, airlines and prices. I see some fares that are two

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Filing Objects to Grid Management Charge

ELCON and eight other customer generator organizations filed a brief at the Federal Energy Regulatory Commission (FERC) taking exception to a recent decision by an administrative law judge that would allow the California independent system operator (ISO) to assess grid management charges on the basis of total potential electricity consumption ("gross load") rather than the electricity actually purchased off the grid ("net load"). The ruling would be extremely costly to existing cogenerators and others who generate "behind-the-meter" in California and could potentially destroy the economic viability of all on-site generation.

"There are numerous facilities in California that generate most of their own electricity," said ELCON's Executive Director John Anderson. "For over twenty-five years, standard industry practice has been to assess grid management charges on the basis of 'net load.' Switching to a 'gross load' standard is unfair, unwarranted, and will, in fact, have negative public policy implications."

Anderson explained, "This ruling is unfair because industrial facilities that generate on-site should not be expected to pay a share of grid management costs that far exceeds the amount of electricity they take off the grid. In fact, in many cases, due to interconnection limitations, it exceeds the amount of electricity they even have the capability to take off.

"It is unwarranted," he said, "because numerous rulings, including one by a different FERC administrative law judge, have assessed charges based on net load. There are no new facts, there is no reason to change long-standing policy."

Anderson said the ruling, if allowed to stand, would contradict and undermine existing national policy and President Bush's National Energy Plan, both of which seek to encourage and expand cogeneration, combined heat and power, and distributed generation technologies because of their superior energy efficiency and environmental benefits. "These fees could add

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Competition has taken a bit of a beating lately...because politicians and regulators tried to hard to ensure that "competition" was all things to all people.

some folks gaming the market - not necessarily breaking the law, but using the law as it existed in ways that had not previously been revealed - to the detriment of consumers.

What bothers me is that as we learn more about alleged market manipulation, we seem to be focusing more on the problems than the solutions.

If we want to start pointing fingers in California and the West, we can find plenty of targets. It's easy to criticize Enron, but the list of people who have helped create a mess in energy markets in California and elsewhere is long.

I suggest we admit that there is enough blame to go around and stop with the recriminations. We don't need to talk end-

Congressional Conferees Will Decide Energy Bill as Fall Campaigns Heat Up

Congressional conferees will meet soon to reconcile a Senate energy bill that includes several electricity provisions in Title II and a House bill (HR 4) passed last May that contains no electricity provisions. This gives the conferees significant latitude in drafting final legislative language. Most observers believe that the conference will not finish its work until just before Congress adjourns in early October -- and that electricity will be among the last issues addressed.

"At present the bill does not contain much to benefit consumers and to promote competition."

"This bill, if enacted, will have a direct impact on how electricity is bought and sold in the United States," said ELCON Executive Director John Anderson. "At present the bill does not contain much to benefit consumers and to promote competition. We will be working to make the bill more consumer friendly as the conference progresses."

The conference equation involves both substantive and political variables. On the substantive side, the Senate bill, passed before market manipulation charges by Enron and other traders were public, contains little market power language. An ELCON-supported amendment from Sen. Maria Cantwell (D-WA) that would have strengthened FERC's market mitigation power was tabled.

Earlier, the Senate had adopted an amendment co-authored by Energy Committee Chairman Jeff Bingaman (D-NM) and Sen. Craig Thomas (R-WY) that limited FERC's ability to take action against market power abuse to no more than current law -- or even reduced FERC's authority, according to some

observers. In exchange for Republican support, Sen. Bingaman promised to oppose any amendments to the electricity section (Title II) of the bill during Senate consideration. However, more recently, Sen. Bingaman was quoted as stating that recent disclosures about market manipulation activities by several power brokers should add credibility to those who want to strengthen market power provisions in conference. House conferees are unlikely to support increased authority for FERC to monitor and remedy market power abuses.

ELCON scored a victory during Senate debate in working to secure passage of an amendment co-sponsored by Sens. Tom Carper (D-DE) and Susan Collins (R-ME) to preserve the rights of cogenerators under the Public Utility Regulatory Policies Act (PURPA). As introduced, the Senate bill would have repealed a utility's obligation to buy cogenerated power and to sell cogenerators backup power. Under the approved amendment, PURPA obligations remain in effect until functioning wholesale and retail markets exist that provide sufficient, available alternatives. Although Sen. Bingaman opposed the

amendment, he accepted it under his agreement with Sen. Thomas and the Republican leadership. But, the amendment will face tough sledding since House conferees will undoubtedly include Rep. Joe Barton (R-TX), chairman of the Energy and Air Quality Subcommittee, who has included PURPA repeal language in numerous proposed bills.

Also on the substance side, ELCON will be working to eliminate -- or at the very least minimize the impact of -- the renewable energy portfolio standard (RPS) found in the Senate-passed bill. This measure would require 10 percent of all electricity to come from new non-hydro renewable sources by 2010. Electricity suppliers not meeting that threshold would be able to buy "credits" (in reality, pay penalty fees which would be passed on to end users in the form of higher rates) from the Department of Energy. During debate, the Senate accepted an amendment from Sen. Don Nickles (R-OK), supported by ELCON, that would reduce the price of such credits from 3 cents to 1 1/2 cents per kWh. Republican House members will likely oppose any RPS requirement.

Conference politics

The House and Senate bills as passed

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House Conferees Selected for Energy Bill

House conferees on the energy bill (HR 4) were appointed from 11 committees, including Energy and Commerce. According to House precedent, only the conferees from Energy and Commerce will address the electricity provisions (Title II in the Senate bill, not included in the House bill). Conferees are:

Republicans

Tauzin (LA)
Bilirakis (FL)
Barton (TX)
Upton (MI)
Stearns (FL)
Gillmor (OH)
Burr (NC)

Democrats

Dingell (MI)
Waxman (CA)
Markey (MA)
Boucher (VA)
Gordon (TN)
Rush (IL)

In addition, Majority Whip Tom DeLay (TX) was appointed to the conference and will presumably participate in debate on electricity issues.

Single Organization Should Set Electricity Standards, ELCON Tells FERC

Electricity reliability and commercial standards must be developed in a single process by a single organization, ELCON told FERC in recent comments. ELCON identified six general criteria that should apply to any standards-setting organization:

1. A single organization must address both reliability and commercial issues, as well as retail and wholesale issues. Reliability and commercial standards (retail and wholesale standards, gas and electric standards) are inextricably linked and cannot be separated. Two organizations working separately will result in continual bickering and arguments over jurisdiction, relationships, and priorities.
2. The process used to set any standard must be ANSI-certified. The American National Standards Institute (ANSI) will not certify a process that is not truly fair, open, balanced and inclusive.
3. A professional, technical standards-drafting staff is essential. All-volunteer processes require tremendous contributions of time from the members. Industrial users and other consumers cannot devote enough staff time to participate adequately in such a process.
4. The staff of the organization should report to an independent board. Sector or segment Boards do not deal well with policy or other difficult issues or interpretations. The problems of the California ISO Segment Board highlight these concerns. NAESB's segment board is a major deficiency.
5. The funding mechanism for any standard-setting organization must be fair and non-discriminatory and not preclude any stakeholder from full participation, yet provide the necessary funds for operations. The Gas Industry Standards Board's \$5,000

fee precludes many from participating, raises concern about the "pay to vote" requirement, and does not raise adequate funds to provide for a professional, technical staff or to compensate independent board members. The North American Electric Reliability Council (NERC) has not established an adequate funding mechanism.

6. Since end-use customers pay all of the bills, they should have a significant proportion of the vote in any governance process. At a minimum, ELCON believes that end-use customers should have at least one-third of the total vote at this point in time. Thus, ELCON recommends a three-segment composition of: (1) producers, (2) transporters, and (3) end-use customers

ELCON also elaborated on ways to create a single process to address both reliability and commercial (as well as

wholesale and retail) electric issues.

The comments were in response to a FERC order in December 2001 requiring "the electric industry" to propose a single standards-setting organization by this past March 15. That has not happened. Both NERC and the recently restructured Gas Industry Standards Board (GISB) -- now the North American Energy Standards Board (NAESB) -- proposed to expand their traditional scopes.

NERC has been establishing "reliability" standards for more than 30 years, but these standards have significant -- often negative -- "commercial" impacts. GISB has been establishing commercial standards for the gas industry for more than five years. The development of standards is important since these standards will become essentially the "rules of the road" for buying and selling electricity.

The comments expanded on filings that ELCON has made during its participation in a number of NERC and NAESB meetings, debates, task forces and workshops. E

ELCON Active in NAESB

ELCON has been active in the North American Energy Standards Board (NAESB) -- formerly the Gas Industry Standards Board (see story this page) -- since it expanded its activities. The group is divided into wholesale and retail electricity quadrants just as it is in gas markets. ELCON has been active in both electricity quadrants since ELCON members purchase electricity in retail markets but consume electricity in a manner and quantity consistent with wholesale markets.

The Retail Electric Quadrant (REQ) has been active, having approved a 2002-2003 business plan and elected officers representing quadrant segments. ELCON Executive Director John Anderson was elected to the Executive Committee as one of four

representatives of the "end user" segment. Other segments on the executive committee are distributors, services and suppliers.

The REQ will focus on issues such as billing and payment, creditworthiness, and metering. ELCON's objective is to ensure that such standards do not discourage competition, especially the ability of consumers to enter into bilateral contracts.

The Wholesale Electric Quadrant (WEQ) has been criticized by several participants, including rural cooperatives and municipal utilities. When operational, it will provide standards on supply and transmission, including scheduling. How NAESB's wholesale quadrant interacts with the North American Electric Reliability Organization is still under discussion. E

ELCON Applauds FERC on Tariff

ELCON strongly applauded a working paper from the Federal Energy Regulatory Commission on standard market design (SMD) that would bring all transmission under a single, flow-based tariff administered by an independent regional transmission organization (RTO). The move would correct perhaps the greatest shortcoming in FERC's policy to promote competitive bulk power markets: the lack of truly comparable access to the interconnected grid for all transmission customers under the same rules, rates, terms and conditions. FERC indicated it recognized the need to reform Order 888's pro forma open-access tariff in a new rulemaking, which will come after comments are submitted on the working paper.

ELCON also commended an idea in the working paper to treat demand response as a resource with rights of access to RTO energy and capacity markets equal to the access traditionally enjoyed only by generation (supply) resources. If a competitive bulk power market is the desired end-state of the Commission's policy, price-responsive demand must have non-discriminatory access to any and all markets (bid-based or otherwise) that are available to generation resources.

At the same time, ELCON urged the Commission to clarify what it expects in the way of compensation for demand resources, a point on which the working paper is silent. In addition, the rulemaking should ensure that prices for demand response are calculated the same way as prices for supply. The prices must not be the result of two separate protocols, procedures or software packages.

ELCON supports other concepts and provisions in the working paper:

- Financial transmission rights (FTRs) would be considered both obligations and options. Existing markets limit FTRs to obligations, which hinders the development of forward markets that are important to retail customers. ELCON supports any effort to develop liquid forward markets that, unlike day-ahead or real-time markets, are more capable of sending price signals for the long-term investments in transmission and generation assets.

- New bidding rules would be developed. ELCON believes that centralized, bid-based markets are particularly vulnerable to generator market power in instances where there is inadequate demand response resulting from the opposition of many states to the participation of retail loads in wholesale markets. States can still trump the intentions of the Commission to create competitive, interstate wholesale markets because of their control over the actions of retail customers.
- Transmission rights would be directly allocated to customers that pay the embedded costs of the transmission system. Of the options being consid-

ered by the Commission, this is the one favored by ELCON. Customers that do not have a direct need for FTRs -- e.g., customers that remain under bundled retail service -- may be better off having them auctioned and accepting the proceeds from the auction to offset any congestion costs they incur in rates.

ELCON supports the working paper's approach to market monitoring and mitigation, which focuses on identifying market design flaws and market rule changes necessary to correct those flaws, and identifying and mitigating anticompetitive behavior and the exercise of market power, primarily economic and physical withholding. ELCON also agrees with a number of concepts underlying FERC'S working paper:

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FERC Working Paper On Flow-Based Tariffs

Revealing a more competitive attitude toward electricity market design, the Federal Energy Regulatory Commission issued a working paper that proposes to replace Order 888's pro forma tariff with a new flow-based tariff applicable to all uses of the transmission system, including bundled transmission to serve native load in "closed" states. ELCON has strongly urged this approach. Highlights:

- Capacity benefit margin (CBM) service--ostensibly needed to access shared reserves from outside the utility's control area but often used to hog available transmission capacity--would come under the flow-based tariff. Utilities would have to procure it on a comparable basis with all other transmission customers.
- FERC would adopt "bid-based security constrained locational marginal pricing" as the theoretical foundation of the market structure. This would include both a day-ahead and real-time spot market.

- Order 888's point-to-point (PTP) and network services would be replaced with a new Network Access Service (NAS) that combines the better attributes of each of the old services: the flexibility and universal access of network service and the reassignment rights of PTP service. This change would support a system of tradable transmission rights that would expand transmission options.

- All transmission customers would pay for any congestion costs (redispatch costs) that are "caused" by their transactions. These costs are only known after-the-fact, meaning that a customer can achieve price certainty only by acquiring financial transmission rights (FTRs) to hedge those costs. The Commission proposed to require the availability on demand of FTRs that are both obligations and options. This is a major victory for transmission customers that do not want the added risk of obligations.

FERC Authority over Transmission Upheld by U.S. Supreme Court

ELCON applauded the U.S. Supreme Court for unanimously upholding the authority of the Federal Energy Regulatory Commission (FERC) to regulate the interstate transmission grid (New York et al v. FERC et al). The court found no statutory language to limit FERC's jurisdiction in the wholesale market.

The court focused on discriminatory practices in the wholesale electricity markets and noted that FERC properly exercised its authority in issuing Order 888. The court recognized that incumbent utilities can and do engage in discriminatory, anti-competitive behavior in their transmission operations. ELCON Executive Director John Anderson said, "Without

using the word, the Court's decision really talked about market power. It is that potential for market power -- the potential for transmission owners to operate the transmission system to keep new suppliers of electricity out of the market -- that is at the core of this decision."

ELCON said that the high court ruling meant that FERC could go further and reverse the simple policy decision in Order 888 not to address bundled transmission rates. In fact, the majority on the court bent over backwards to state that, if FERC developed a record showing discrimination exists in bundled retail sales, it would have the authority and the duty to address such a problem. **E**

Management Charge

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expenses of over \$2 million annually to a 50-megawatt load served by internal generation," he said. "That would probably make the project non-viable, likely forcing the industrial generator to close the facility."

ELCON was supported in its brief by the United States Combined Heat and Power Association, the American Chemistry Council, the American Iron and Steel Institute, the American Forest & Paper Association, the American Petroleum Institute, the National Petrochemical & Refiners Association, the Fertilizer Institute, and the Chemical Industry Council of California. A full copy of the brief is available at www.elcon.org under "FERC Filings." **E**

Flow-Based Tariff

From Page 5

- Structural remedies are superior to behavioral remedies.
- Mitigation before the fact is preferable to retroactive price changes. Industrial consumers that often make costly decisions based on an expected price can be seriously harmed if prices are retroactively revised. For example, demand response becomes almost unworkable if there is a chronic risk of after-the-fact downward price adjustments.
- Energy and transmission markets must accommodate and expand customer choices. Buyers and sellers should have options such as self-supply, long-term and short-term energy and transmission acquisitions, financial hedging opportunities, and supply or demand options.
- Market rules must be technology- and fuel-neutral. They must not unduly bias the choice between demand and supply resources or provide competitive advantage or disadvantage to large or small demand or supply resources. Demand and intermittent supply resources should be able to participate fully in energy, ancillary services, and capacity markets.

- Demand response is essential in competitive markets to ensure the efficient interaction of supply and demand, as a check on supplier and locational market power, and as an opportunity for choice by wholesale and end-use customers.

Solutions that increase the potential number of suppliers or increase price-responsive demand must be promoted.

- The demand side must be able to participate in energy markets. The demand side can participate as buyers or sellers (e.g., offering to sell operating reserves). A buying entity must be able to submit bids that indicate it is willing to vary the quantities it purchases based on prices that it may be charged.
- Sellers (including demand side) must have the option of submitting multi-part bids -- e.g., submitting separate but related bids for start-up costs, no-load costs and energy.
- The demand side must be able to participate in the real-time market.

- Demand must have the opportunity to supply operating reserves if it meets the necessary operational requirements (which should be designed to enable demand response participation).
- Demand-side supply of operating reserves must have non-discriminatory bidding opportunities in the market.
- Market forces such as supply and demand responses are the most potent and lasting means of mitigating generation market power, so solutions that increase the potential number of suppliers or increase price-responsive demand must be promoted. **E**

Yacker Elected NERO Chairman

ELCON Director of Government and Public Affairs Marc Yacker was elected chairman of the National Energy Resources Organization (NERO) for 2002-03. The chairman is NERO's chief officer. Yacker had served as president for the past year. NERO is a nonpartisan organization whose purpose is to foster constructive dialogue on energy policy issues. NERO members come from all segments of the energy community. **E**

Highlights of ELCON's 26th Annual Meeting in Las Vegas

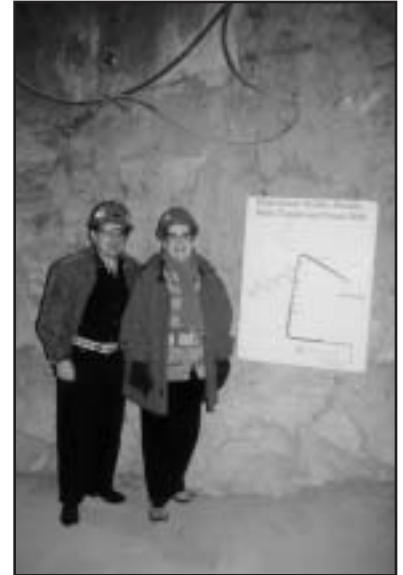
ELCON held its 26th annual meeting this year in Las Vegas, Nevada. Highlights were a tour of the proposed nuclear waste depository at Yucca Mountain and a Members Only Workshop on standard market design and best practices.

Some 30 ELCON members toured Yucca Mountain, located about 100 miles from Las Vegas in a remote area with a deep-water plain, making it ideal for nuclear waste disposal. Under federal law, the U.S. Department of Energy has been conducting a series of tests to determine whether nuclear waste can be transported here and safely stored underground. The waste is being housed temporarily at more than 100 sites around the nation.

Coincidentally, within days of the

ELCON tour, President Bush announced that he was officially recommending Yucca Mountain as the government-designated site for nuclear waste disposal. The decision was challenged by Nevada Governor Kenny Guinn and will be decided by Congress.

The ELCON workshop featured presentations by Jim Dauphinais of Brubaker Associates and Scott Miller of the Federal Energy Regulatory Commission. They described various options in market design and various ways regional transmission organizations (RTOs) could address congestion. ELCON members continue to support transmission models that promote competition, take into account commercial implications, and provide transparency to purchasers. **E**



Above: ELCON Executive Director John Anderson and wife Mary Jo inside mountain.

Below: (l-r) Greg Dorriety, Silicon Energy; Steve Breckon, Williams Energy; Lloyd Webb, Eastman Chemical; and Marc Yacker, ELCON, in the 1st ELCON Open Golf Tournament. *Bottom left:* Tunnel borer.



FERC Denies PJM Price Complaint

The Federal Energy Regulatory Commission issued an order denying a complaint by The New Power Co. that prices in the PJM Interconnection are unfair. ELCON had supported New Power's complaint.

PJM recently imposed a seasonal penalty on generators that fail to meet its reserve capacity requirements. New Power asked the Commission to eliminate the deficiency penalty and instead to

require PJM to use a daily penalty and order refunds. The Commission denied the complaint because New Power failed to demonstrate that prices for capacity in PJM are unjust and unreasonable or unduly discriminatory. FERC said it wanted to support PJM's installed capacity (ICAP) responsibility, which it said helps ensure there is sufficient capacity to meet peak needs at prices for reserve capacity that are just and reasonable. **E**

Iceberg

From Page 1

-- skyrocketing prices and a high likelihood of rolling blackouts."

"California created just such a scheme, and they taught the rest of us a lesson I hope we never forget," Anderson said.

"FERC is creating markets facilitated by ISOs and RTOs faster than it is creating market rules," Anderson said. "The

Commission must define and enforce specific rules for bidding behavior before these markets are allowed to operate. It should not put the cart before the horse."

"Consumers get hurt," Anderson continued. "It doesn't make any difference if the consumer is residential or industrial -- those high prices hurt. Given the interstate nature of the grid and interstate business practices these companies have engaged in, we can only look to the federal government for redress." **E**

Conferees

From Page 3

are not very much alike. Differences over such controversial issues as electricity provisions and exploration of the Arctic National Wildlife Refuge (ANWR) will require lengthy negotiations. To further complicate matters, the Senate Democrats appointed as conferees are not from the Energy Committee, as tradition would dictate, but, for the most part, are instead chairmen of other committees. These Senators were active in the energy debate only on isolated sub-issues and are not really energy legislators. Some observers believe that some of these Senators want to develop a campaign issue to benefit Democrats (such as the development of ANWR or stricter auto fuel efficiency standards) rather than craft a comprehensive bill.

Questions hang over the conference. What does the Administration hope to see in the final package (having said that ANWR exploration is important but not essential), and what is it willing to accept in a final package? Will some Democrats push a pro-environmental bill

on the President, daring him to veto it? What about those Democrats content with increasing the rhetoric and not producing a bill at all?

Another question concerns the timing of the negotiations. If, as most suspect, the conference is not concluded until late September or early October, the political landscape will look quite different than it does now. Members of both parties will be watching House and Senate races that could decide the majority next year.

For example, Sen. Tim Johnson (D-SD) will likely be in a tight campaign for re-election. Will Senate Democrats feel impelled to include an ethanol provision benefiting South Dakota? Similarly, Sens. Bob Smith (R-NH) and Susan Collins (R-ME) are likely to have strong opponents. Both have made a point of their opposition to ANWR. Will the Republican leadership back off support for ANWR language so as not to harm the political chances of their two New England colleagues?

Will politics triumph over substance? The ending is far from clear. Anyone who thinks he or she knows the answer probably has not considered all the variables. **E**

Letter to FERC

From Page 1

(RTOs) and independent system operators (ISOs) have been approved.

"FERC has a duty to protect all customers, regardless of whether they reside or do business in an RTO/ISO," according to the letter from ELCON, Transmission Dependent Utility Systems, American Public Power Association, National Rural Electric Cooperative Association, American Forest and Paper Association, and Transmission Access Policy Study Group.

The letter noted that the Bush Administration's policy related to Enron is to support tough enforcement of laws that protect consumers, adding, "It is difficult to conceive of a consumer protection more basic than one providing for refunds when markets have been manipulated to the detriment of those consumers."

The letter argued that since FERC recognizes that market power abuse can and does exist, and since it created a refund obligation as a condition of market-based rates, the Commission must use the refund mechanism whenever necessary to protect consumers.

Furthermore, market power problems "exist in all nascent markets," the letter said. "The fact that an RTO has been initiated does not mean that there is a liquid market."

For example, the New York, Connecticut, Michigan, and New England public utility commissions; the attorney generals of Rhode Island, Massachusetts, New York and New Mexico; and the California Electricity Oversight Board all advocated FERC's proposal, or a stronger variant, the letter noted.

Bid-based markets are "vulnerable to abuse -- not only by a single company and not only in a single state," the letter said. FERC must continue to address market problems in wholesale electricity markets until there is adequate evidence of competition -- i.e., many buyers, many sellers, adequate infrastructure and ample market information on price, terms and quantity. If these are not present, then the existence of an RTO, ISO or centralized bid-based market will make little difference. **E**

AEP/CSW Merger Rejected by Court

The U.S. Court of Appeals for the D.C. Circuit ruled that the merger of American Electric Power and Central & Southwest (CSW) violated the Public Utilities Holding Company Act (PUHCA) (NRECA and APPA v. SEC, No. 00-1371). PUHCA requires registered holding companies to comprise a "single integrated system" that is "physically interconnected or capable of interconnection" and "confined in its operations to a single region."

AEP and CSW's systems are neither contiguous nor physically interconnected. The companies undertook to interconnect their systems by means of a 250 MW, unidirectional transmission contract with Ameren for four years. SEC approved the merger on the basis that the contract path satisfied PUHCA integration requirements. The National Rural Electric Cooperative Association and American Public Power Association sued.

The D.C. Circuit rejected two of the lawsuit's challenges -- that the contract path was too small and the merger applicants were too tentative on their integration plans once the contract expires in 2003. However, the court agreed with NRECA/APPA that the unidirectional contract path violated the Webster Dictionary definition of "interconnection." This term requires "mutual connection" or two-way transfer of power.

The court also ruled that SEC failed to explain a change in its past policy of holding that a contract path alone cannot integrate distant utilities.

The court held that AEP and CSW are simply not in the same region. Institutional and technological improvements "may well justify ever-expanding electrical utilities, but PUHCA confines such utilities to a 'single area or region.'" The court took note of pending legislative proposals to repeal PUHCA. Unless and until Congress acts, the Commission "may not rule out of the act the requirement that registered holding companies be confined to a 'single area or region.'" E

ELCON Chair

From Page 2

or three times the price of others. I know that competition is working.

I know that competition is working every time I make a long distance call. As one who is old enough to remember when making or receiving a long distance call was a major event ("Quick, get off the phone, Uncle Joe is paying for this"), the low rates we take for granted today are just one bit of evidence that competition is working. Similarly, every time I make or receive a call on my cell phone, I thank my lucky stars that competition is working.

In electricity, competition clearly is not working - yet. That may be, as I suspect, because the proposals put forth by legisla-

tors and regulators were not really proposals for competition. It may also be that there is a learning curve - one for sellers of electricity figuring out how best to market their product and another for consumers of electricity trying to understand what products they need or want.

I simply ask that competition not be dismissed quickly or summarily. California's plan didn't work. Enron's actions were duplicitous and some say illegal. But that should not deter us from seeking the most efficient electricity system we can possibly construct. And I continue to believe that competition must be at the foundation of that system.

Carol Hyams Guthrie is General Manager, Electric Market Strategies, ChevronTexaco

Refunds

From Page 1

the consequences of violating those rules) are not known in advance, the comments said. It is not the Commission's responsibility to reduce investment risk by shifting such risk to customers by condoning prices that are not just and reasonable.

Equally important, FERC has a duty to correct flawed market structures, according to the comments. For example, the

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consensus is almost universal that workably competitive wholesale markets require a robust demand response, yet no credible market for demand response exists today -- not even within approved, independent system operators (ISOs) or regional transmission organizations (RTOs). Thus, the prices set in those markets are not just and reasonable. ELCON

supports the Commission's efforts to correct this problem. (FERC's proposed "Working Paper on Standardized Transmission Service and Wholesale Electric Market Design" is encouraging.)

There is no way, at this time, to identify all examples of economic or physical withholding, anticompetitive behavior or exercise of market power, ELCON said. The wholesale markets are relatively new, and new forms of trading behavior, both competitive and anticompetitive, are emerging as traders gain experience with these market structures. It is essential that a substantial refund risk be in place to act as a deterrent against truly anticompetitive behavior and the exercise of market power, the comments said.

The burden of proof that a supplier did not engage in economic and/or physical withholding is with the supplier, the comments said. When a supplier is suspected of such behavior, it must fully document any legitimate environmental, operational and/or reliability factors that created the perception of anticompetitive behavior or the exercise of market power.

ELCON also warned against including "legitimate and verifiable opportunity costs" in any assessment of a supplier's full incremental costs, which will lead the Commission rapidly down the slippery slope of administratively determined prices--more appropriately called rates. E

ELCON Activities Before The Federal Energy Regulatory Commission

ELCON and four public power and transmission-dependent electricity organizations urged the Federal Energy Regulatory Commission to go further than the ideas laid out in a thought paper by FERC Chairman Pat Wood on ways to address generation market power by utilities.

Wood's "strawman" concept paper described his current thinking on a number of issues related to the market-monitoring responsibilities of regional transmission organizations (RTOs) and structural and behavioral policies for mitigating market power of generators and transmission owners. Wood's ideas include expanding the authorities and responsibilities of each RTO's Market Monitoring Unit ("MMU") and implementing price mitigation mechanisms.

Those ideas may not be enough, according to ELCON and the other organizations (American Public Power Association, National Rural Electric Cooperative Association, the Transmission Access Policy Study Group, and the Transmission Dependent Utility Systems). They recommended additional steps, including the following:

- FERC should carefully consider comments recently filed by the Federal Trade Commission that stressed the shortcomings of relying on antitrust enforcement to curb market power in the electricity markets. According to the FTC, "because electric power is sold on an hourly basis, market dynamics - and thus the incentive and ability to exploit market power - can shift over the course of each day, making it virtually impossible to intervene before conditions have changed."
- The formation of RTOs and ISOs is crucial to preventing market power,

but they aren't the sole remedy. The Commission needs to conduct region-by-region economic analyses of prospective RTO markets for energy, capacity, redispatch and ancillary services. Generators should not be given market-based rate authority for such services if insufficient competition exists in a region to restrain the prices the dominant generator can charge for the service. This should apply even if an RTO has been formed in the region. Appropriate mitigation measures should be attached to any pricing authority that is provided.

- The California experience proves that the presence of an ISO and external market monitors will not prevent the exercise of market power. The Commission cannot forego regional market economic analyses on the assumption that the mere presence of an RTO, a market monitor, and/or an RTO-run centralized, bid-based market will cause a competitive generation market to spring up.
- The Commission must conduct, either in the relevant market-based rate or RTO dockets, a region-by-region examination of generation markets, including the universe of possible competitors, transmission constraints on the boundaries and within the RTO footprint that might cause the market to splinter into submarkets or load pockets, peak and off-peak demand and supply, and potential suppliers of different types of service (firm load-following service, ancillary services, etc.).
- Demand-side response is necessary but not sufficient to prevent the exercise of market power. A substantial portion of end-use customers' demand

will remain inelastic despite the opportunities that demand-side response will provide.

- The Commission must not only focus on sustained events but also address the transitory exercise of market power. Transitory price increases of great magnitude can inflict as much damage as sustained price increases of lesser magnitude, and both should be taken equally seriously.
- The Market Power strawman suggests that the Commission wants to avoid engaging in refund mitigation measures. FERC must remember that refunds are at the heart of the consumer protection scheme in the Federal Power Act, regardless of whether it is a disruptive mitigation technique.

The National Association of State Utility Consumer Advocates (NASUCA) submitted a filing supporting ELCON and the other groups. To illustrate the point that the presence of an RTO is no guarantee generators won't attempt to exercise market power, NASUCA reminded the Commission that it took the PJM interconnection three months to remedy design flaws that had allowed a generator in the region to exercise market power.

Interconnection Standards

ELCON raised four concerns with FERC's proposed rule on standardized generator interconnection agreements and procedures:

1. Instead of creating two interconnection standards -- for "energy resources" and "network resources" -- FERC should adopt the Minimum Interconnection Standard approved for the New England Power Pool

(NEPOOL). FERC said the two generator types would be subject to different upgrade responsibilities and accorded different rights to dispatch. ELCON said such a dual system perpetuates the notion that the "transmission grid is the property of incumbents rather than a public resource funded by ratepayers to be allocated to those resources who serve ratepayers' needs at lowest cost. Any standard that requires a new generator to incur additional costs in order to be considered a 'Network Resource' perpetuates a preference for incumbent use of the system."

2. FERC should preserve state authority over cogenerating facilities qualifying under the Public Utility Regulatory Policies Act (PURPA). Qualifying facilities are not merchant generators and should not be regulated as such.
3. Rights under existing interconnection agreements should be preserved and carried over upon termination of the agreement absent some "material change" in the interconnection. Even in that case, the generator should not be considered a brand new facility for purposes of cost allocation.
4. FERC needs to recognize that customer generators are not merchant generators and the interconnection agreement must strictly limit the potential for curtailment or redispatch of any generator that is integrated with an industrial process.

ELCON said it agreed with FERC that good interconnection standards and procedures will encourage needed investment in infrastructure, limit opportunities for transmission providers to favor their own generation, and ease entry for competitors while ensuring efficient siting decisions.

Over the next several years, the comments noted, a few large regional RTOs will come into existence with standard market designs and new, conforming reliability standards and commercial practices. It is important not to confuse the

Self-Generators Serve All Electricity Users

From ELCON's Comments On Interconnection Agreements

"A workably competitive wholesale electricity market requires the elimination of entry barriers to new generation in all its forms, including on-site customer generation that intends to serve all or part of a customer's "behind the meter" load. All end-use consumers benefit from customer generation whether or not they own or operate it. In a competitive wholesale market, the economic viability of some loads to self-generate puts downward pressure on market clearing prices that everyone pays. As it becomes more expensive to self-generate, i.e., as opportunity costs increase, all consumers become vulnerable to higher prices."

"All generators should be intercon-

ected to the system on a basis that preserves the reliability and stability of the system and does not degrade the total transfer capability available to serve consumers. Thereafter, each generator must be free to compete on the basis of price with other generators...."

Confusing the issue of overall system planning with the requirements for generator interconnection leads to economic inefficiency, barriers to entry, subsidies of incumbent generators, interferes with rational planning and expansion by the RTO, delays needed expansion of the transmission system and/or runs the risk of redundant and unnecessary investment.

unique needs of customer generation with merchant generation, since that could create new barriers -- or preserve old ones -- inhibiting the development of customer generation.

In earlier comments on FERC's initial, advance notice of rulemaking on this issue, ELCON said it agreed with the several positions voiced by generators:

- securing interconnection without requesting delivery is difficult,
- new generators are not treated the same as a transmission provider's own generators,
- system upgrade costs charged to generators are sometimes not related to the interconnection,
- delays and uncertainty occur due to the lack of binding commitments and firm deadlines in transmission providers' pro forma tariffs, and
- there is a lack of transparency of transmission information needed to make an independent assessment of the impact of an interconnection request.

ELCON noted that FERC's November

2000 reports on regional bulk power markets identified the adverse effects of uncertainty and delay in processing generation interconnection requests. The mere act of standardization minimizes the potential for discriminatory procedures or requirements that are too often invoked to discourage on-site generation.

ELCON has participated in meetings between large and small generators, transmission providers, state agencies and transmission-dependent utilities to develop standard generator interconnection precedents and a standard generator interconnection agreement. In a January filing, the leading groups identified differences in position between the generation groups and the transmission owners. ELCON supports the position of generators and small generators on interconnection requests, OASIS posting, coordination with affected systems, queue positions and the Small Generator Expedited Interconnection Study language -- in other words, where there is divergence of opinion vis-à-vis the transmission owners. E

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WHAT IS ELCON?

- **DATE ORGANIZED:** January 15, 1976
- **WHO WE ARE:** The Electricity Consumers Resource Council (ELCON) is the national association representing large industrial consumers of electricity. ELCON was organized to promote the development of coordinated and rational federal and state policies that will assure an adequate, reliable and efficient supply of electricity for all users at competitive prices. ELCON's member companies come from virtually every segment of the manufacturing community.
- **MEMBER COMPANIES:** A.E. Staley Manufacturing Company • Air Liquide • Alcan Aluminum Corporation • Anheuser-Busch Companies, Inc. • BOC Gases • BP • Central Soya Company, Inc. • Chevron Texaco • Delphi Automotive Systems • E.I. du Pont de Nemours & Co. • Eastman Chemical Company • Equilon Pipeline, L.L.C. • ExxonMobil • FMC Corp. • Ford Motor Company • GNB Technologies • General Motors Corporation • Honda • Honeywell • Intel Corporation • International Paper • MG Industries • Monsanto Co. • Occidental Chemical • Owens-Corning • Praxair • Rockwell Automation • Smurfit Stone Container Corp. • Solutia, Inc. • Weyerhaeuser • Williams Energy Services
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