

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

REMOVING OBSTACLES TO
INCREASED ELECTRIC GENERATION
AND NATURAL GAS SUPPLY IN THE
WESTERN MARKETS

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Docket No. EL01-47-000

MOTION TO INTERVENE AND
COMMENTS OF INDUSTRIAL CONSUMERS

In this docket, FERC announces a series of initiatives to relieve the crisis in the Western markets, including actions to encourage demand reduction. Industrial Consumers, the Electricity Consumers Resource Council (ELCON), the American Iron and Steel Institute (AISI), the American Chemistry Council (ACC), and the American Forest and Paper Association (AF&PA) welcome FERC's initiatives to encourage demand-responsive load as a viable resource, separate and apart from traditional generation resources. Industrial Consumers also submit comments on other proposals in the Commission's March 14, 2001 Order.

EXECUTIVE SUMMARY

Short-term measures: Industrial Consumers strongly support the proposals in FERC's March 14, 2001 Order that would provide a "blanket authorization" of market-based rates for those end-users that are capable of reducing their consumption by reducing on-site demand, increasing onsite-generation, or a combination of the two. Industrial Consumers

recommend that any verifiable demand reduction should be exempt from prevailing price or bid caps which were instituted due to the lack of viable demand response. Utilities or Load Serving Entities (LSEs) have no entitlement to share in the economic benefit of such transactions. While the March 14, 2001 Order is directed at problems in the Western markets, there is compelling need for similar measures in the Eastern Interconnection.

Long-term measures: In these comments, we propose consideration of a new RTO “Function 9” -- curtailable load response -- whereby RTOs would allow large commercial and industrial consumers (or other customers through aggregators) to resell their load into short-term wholesale markets and receive a market price for this resource. Customers are now capable of being active participants in the electricity markets and in the real-time power system operation and control. Load response from large customers could play a significant role in maintaining the real-time energy balance and system reliability. The current development of RTOs throughout the country provides the perfect vehicle both for enabling industrial customers to participate in electricity markets and for developing rules and regulations that require their equal participation in all markets. Programs to date focus on the need to provide demand-response resources in a pending reliability emergency. In more established markets, voluntary, price-responsive load can be expected to enter the market at any time, reflecting the opportunity costs of the customer.

Industrial Consumers urge FERC to convene a technical conference so that stakeholders can explore implementation of Curtailable Load Response (CLR) as a ninth RTO function. Through a combination of voluntary RTO initiatives and modest revision to open access tariff requirements, markets for CLR services can readily be established.

Need For A West-Wide RTO: California ISO (CAISO) has dragged its feet in agreeing to a regionwide RTO, and its latest filings provide no justification for its continued refusal to take the necessary steps to ally with RTO West and Desert Star. Industrial Consumers support the formation of a west-wide RTO, subsuming the entire Western Interconnection, and urge the Commission to actively promote the consolidation of the California ISO with other RTOs that are under formation in the West.

Other Issues: Industrial Consumers also support several other provisions in the March 14, 2001 Order, including (i) the extension of waivers for Qualifying Facilities (QFs) to allow increased generation; (ii) the adoption of streamlined regulatory procedures to accommodate wholesale sales from existing on-site generators, and to increase generation resources in the West; and (iii) the proposal for FERC to exercise its Section 210(d) authority under the Federal Power Act to “alleviate any existing impediments” associated with the physical interconnection to the grid of any cogeneration, small power production, or transmission facilities, and thus preventing generation resources from reaching load.

COMMENTS

I. INDUSTRIAL CONSUMERS’ COMMENTS ON SHORT-TERM MEASURES TO ADDRESS DEMAND RESPONSE

A. The Need For Demand-Response Measures Is Not Limited To The West

The Commission’s March 14, 2001 Order is primarily directed at mitigating potential supply shortfalls (*i.e.*, power outages or “blackouts”) during the coming summer peaking season in California (and the West, in general). But this problem is not limited to the West. The Northeast and other regions in the Eastern Interconnection are also at risk because

every sub-region within the Interconnection is electrically “interconnected” with every other sub-region or market, and thus, a problem in one region can cascade to others, regardless of the nominal generating capacity locally available.¹ The divestiture of generation and partial deregulation of the generation market has created new market and reliability risks that federal and state regulators, and the North American Electric Reliability Council (NERC), are just beginning to comprehend.

In the Eastern Interconnection, part of the problem results from NERC’s crude Transmission Loading Relief (TLR) procedures. FERC has recognized that TLR is an inefficient, unpredictable and imprecise tool to address transmission congestion. Other problems in the East result from the balkanization of markets following state restructuring efforts, and the establishment of small ISOs in the Northeast. These ISOs have insular operating practices and market designs that prevent them from coordinating their operations with the rest of the interconnected grid, and thus, operate on a “beggar-thy-neighbor” basis, even if not intentionally.

The Western Interconnection has a more complex situation, derived mostly from the following core problems: (1) an acute shortage of new generating capacity necessary to meet recent demand growth; (2) an unfortunate market design in California, the largest regional market in the West; and (3) unfavorable weather that prevents reliance on the West’s traditional

¹ See, for example, “Power Alert, New York’s Energy Crossroads,” A Report by the New York Independent System Operator, March 2001. The report can be downloaded from: http://www.nyiso.com/topics/articles/news_releases/power_alert_wp.pdf

standby, its hydroelectric resource base. The West's problems have also been exacerbated by extremely high price increases for natural gas and air emission offsets, which may not be totally unrelated to the core problems.

There is almost universal agreement that some form of demand-responsive engagement in wholesale spot markets is essential for establishing workably competitive electricity markets. Markets with only a supply-side (i.e., *wholesale-only* markets) are not true markets. Every economics textbook displays intersecting "supply" and "demand" curves with each sloping in opposite directions to connote the different willingness to buy or sell of different buyers and sellers, respectively. Yet, most restructuring efforts in the United States, at either the federal or state level, focus almost exclusively on a wholesale-only market, with at most, token integration of demand with supply as required by basic economic principles. Hence, Industrial Consumers applaud the Commission's and the Commission Staff's continued vigilance on this issue.

B. Industrial Consumers Strongly Support FERC's Proposal Concerning "Purchases Of Demand Reduction"

The "blanket authorization" of market-based rates for such demand reductions will encourage many price responsive end-users to participate in special demand reduction programs that are offered by ISOs and utilities in anticipation of tight supply situations this summer. The blanket authorization helps create some certainty that end-users that are capable of reducing their net consumption from external resources (by reducing on-site demand, or increasing on-site generation, or a combination of the two) are fairly compensated for their actions. By tying the compensation to "market-based rates" (and presumably, actual market clearing prices), the economic incentive to participate is also maximized without recourse to

subsidies or other artificial inducements. This holds non-participants harmless to such transactions, while maximizing efficient trading activity.

Load curtailment is not free of costs. Many loads will incur substantial out-of-pocket costs to curtail load that is unrelated to the actual price of the power. Hence, any participation in a market for demand reduction must at least compensate the participating load for these out-of-pocket costs. Efforts to reduce the payment—by whatever means—only limit the number of participating customers and the amount of load that “trades” in the short-term market. The most efficient way to maximize participation rates and the volume of load bid, is to allow the trading at market clearing prices.

C. Industrial Consumers Recommend That Any Measurable And Verifiable Demand Reduction Be Bid Into An ISO Or Utility Program Exempt From Bid Caps

In each regional market that is most at risk of supply shortfall this coming summer, FERC has imposed price or bid caps on supply resources eligible to enter the market. This includes markets operated or facilitated by CAISO, PJM, New York ISO, and ISO New England. Price caps were imposed because there was no demand response in the applicable market, a quintessential requirement of a workably competitive market. These markets were, and remain, *wholesale-only* markets in which the generators (unrestrained by competition from reduced demand) can exert substantial market power and drive market prices to levels that more than allow a competitive return of, and on, their investments. If the imposition of price or bid caps was predicated on the absence of any meaningful demand response, then it clearly makes no sense to subject any ensuing Demand Reduction to whatever price or bid cap that is currently enforced on generators or marketers. The only legitimate purpose of a cap is to

restrain uncompetitive behavior. Imposing the same caps on demand responsive bids will only restrain the availability of this resource for the purpose of correcting the market failure.

D. End-Use Customers That Elect To Bid Demand Reduction Resources Into Local Wholesale Spot Markets Should Not Be Obligated To Share The Savings With Their Traditional Retail Suppliers

Many demand response programs offered by utilities or Load Serving Entities (LSEs) require the customer to share their savings with the utility or LSE. A fifty-fifty split is not uncommon. The ability, or audacity of the utility or LSE to suggest such accommodation has no precedence in other competitive commodity markets. It is a vestige of the expectations and market power of a monopolist or monopsonist.

If the customer has title to firm delivery of energy (whether by contract or tariff), it may, at its own discretion, resell that entitlement unless the contract or tariff explicitly prohibits such resale. However the customer mixes and matches its own requirements, including substituting purchases from the grid with on-site generation, should be of no concern to any other market participant. The local utility is not entitled to its “cut” of the transaction by virtue of its traditional market power.

E. FERC Should Encourage Utilities To Wean Themselves Off Of Unearned Revenues That Were Guaranteed Under Traditional Regulation

Under traditional regulation, utilities (including their recent reincarnations, such as LSEs) have assumed an expectation that their revenue requirement is an inviolate entitlement, immune from normal business risk. They assume that any business risk that reduces their income should be fully compensated, and they should be made “whole.” In the context of the circumstances leading to the Commission’s immediate inquiry, utilities continue to presume that they should be immunized from any financial risk resulting from lost sales. Thus, any program

intended to prevent widespread power blackouts in any region must compensate the local “wires” company for lost revenues resulting from voluntary customer load curtailments that would help prevent such outages. We urge the Commission not to encourage such selfish expectations.

F. Industrial Consumers Response to December 15 Directive

The Commission seeks comments on the desirability of accelerating a “long-term” directive in its December 15 Order on California issues. In that Order, FERC directed as a “longer-term measure” that CAISO pursue establishing an integrated day-ahead market in which all demand and supply bids are addressed in one venue.

Industrial Consumers strongly support any acceleration of the development of fair and workably competitive electricity markets. However, we do not believe that the best solution can be achieved in time to meet Summer 2001 contingencies. There is simply not enough time. Ideally, the appropriate “venue” is the RTO and its RTO Function 4 requirements (ancillary services including a real-time balancing market).² As explained immediately below, we propose a new RTO Function 9 to provide the necessary integration. However, we strongly urge that this market NOT be limited to, or mandated as a “day-ahead” market. The decision to enter a day-ahead market must rely on forecasts of next day events. The decision to enter a “day-of” market, or near real-time market, will rely on facts not forecasts. Prices in real-time markets also tend to be higher than forecasted on a day-ahead basis. Thus, if the intent is to maximize entry into the demand reduction market, then the market must not be restrictive. Tradable loads should be traded on the same basis as generation and the ability to provide the

² The ancillary functions specified in RTO Function 4 do not include demand response.

resource in forward contracts and short-term bids in various ancillary service markets should not be artificially restricted. The number one lesson from California that all regulators should be mindful of is beware of the unintended consequences of undue restrictions.

II. LONGER TERM MEASURES: FERC SHOULD CONSIDER A NEW RTO “FUNCTION 9” TO ACHIEVE ITS OBJECTIVES ON DEMAND RESPONSE

A. Need For A Market for Customer Load Response (CLR)

The electricity markets in the United States are developing complex and sophisticated mechanisms for generators, transmission owners, energy marketers and other participants on the supply side of the market. Customers, however – from residential consumers to large industrial load centers – only become aware of these advances by virtue of higher electricity prices. Customers have not yet been given the opportunity to participate in the markets at a level equal to that of generators and other suppliers. The failure to include mechanisms for demand response in the initial markets is now recognized to be a significant and unfortunate oversight on the part of market designers and participants. A market cannot function without participation from the demand side. The electricity markets emerging throughout the country are failing from the lack of mechanisms to allow voluntary demand response from customers.

The current development of RTOs provides the perfect vehicle both enabling industrial customers to participate in electricity markets and for developing rules and regulations that require their equal participation in all markets. If FERC does not require RTOs and other transmission providers to purposefully incorporate demand-responsive load services into both their open access tariffs and market designs, electricity markets and the industry restructuring

will continue to flounder. In addition, markets for this service must be reasonably standardized to facilitate efficient trading and liquidity within and through RTOs.

Existing demand response “programs” are only a temporary expediency, and must be replaced, as soon as possible, with “markets” for such services. Demand responsive load is not strictly an “emergency” service, but an essential requirement of a competitive electricity market. The programs proposed by CAISO, PJM, and New York ISO, in the short term, are important steps in the evolution to such competitive markets. Nonetheless, these programs should be supplanted with the real thing as soon as possible.

While demand responsive load can help mitigate potential supply shortfalls, the real value of this service is to enable the formation of a highly efficient market for trading and balancing supply and demand. This should minimize or eliminate the need for price caps or artificial markets for “capacity.” The long-term concern is not whether all retail customers “see” real-time spot prices. The real concern is whether markets are sufficiently structured to enable certain price-responsive loads to voluntarily adjust to real-time prices.³

B. Customers Are Now Capable Of Demand Response

Traditionally, power systems have operated based on the assumption that generation was controllable while load was stochastic and uncontrollable. To maintain the desired frequency and voltage profiles, power systems relied upon sophisticated design and control technologies for generation, with only minimal attention given to developing comparable

³ All retail load need not participate directly in the wholesale spot markets, in fact, retail loads should not be forced into any market. That is not the intent “customer choice” or competitive markets in general. As in other wholesale commodity markets, only a fraction of the demand need be directly engaged in the spot market. Thus, only those entities with the requisite skills in price and risk management need participate. This does not preclude small retail customers from participating through market intermediaries such as aggregators.

technologies for load. This traditional model is no longer appropriate for a competitive industry that emphasizes market participation, and is no longer necessary given the advances in metering, communications, and control technologies for loads.

Large industrial and commercial customers are also increasingly likely to have on-site generation that could become an important source of energy and ancillary services in the market-oriented power industry. Customers, with or without on-site generation, are capable of supplying energy to the balancing and congestion management markets through increment and decrement bids, participating in energy reserves, and assisting in frequency and voltage regulation. Retail customers, however, are prevented from participating in electricity markets in a manner equal to that of generation because institutional and regulatory barriers persist. To overcome these barriers and successfully integrate demand responsive load into RTO markets, customers must receive equitable value for their participation while being able to standardize the trading procedures across multiple sites. To this end, Industrial Consumers urge the Commission to consider the establishment of a new RTO Function 9 for the express purpose of integrating demand response and supply bids into short-term markets.

C. FERC And FERC Staff Have Recognized The Need For Demand Response

Volatile prices and supply shortages, though most visible in California and other Western states, have been recurring problems in electricity markets throughout the country. In evaluating these events, FERC Staff Reports and Orders recognize the potential for customer load response to address market crises in California, New York, and the Midwest.

- FERC Orders On The California Crisis: In FERC's November 1, 2000 Order in the San Diego Gas & Electric proceedings, 93 FERC ¶ 61,121, FERC recognized lack

of demand responsiveness of retail load as one of the primary contributing factors to the supply-demand imbalance in California. This conclusion was reiterated in FERC's December 15, 2000 Order, 93 FERC ¶ 61,294. FERC directed "the ISO and Scheduling Coordinators to consider demand bidding programs in which loads can bid offers of demand reduction directly into the market to compete with offers of supply." Id.

- FERC Staff Report On Western Markets: The Staff Report on the "Western Markets and the Causes of the Summer 2000 Price Abnormalities" states, "In well functioning competitive markets, both suppliers and consumers are able to see and respond to market prices. Indeed, this is what allows competitive markets to achieve the efficient outcomes for which they are well noted. However, in electricity markets, such as those of California, consumers often must make their consumption decisions without knowledge of the true market price of electricity. In addition, some utility purchasers of electricity, such as SDG&E, may not always have strong incentives to minimize the wholesale cost of the electricity that they purchase for their retail customers. This lack of demand responsiveness can, at times, lead to excessively high prices. . . . It appears difficult to develop a large amount of demand response, but the reasons appear to be institutional more than physical." FERC Staff Report, November 1, 2000, Chapter 5, Section 2, page 5-10, 5-11.

FERC Staff concluded that FERC should provide more demand response to wholesale pricing. Specifically, FERC should:

- Encourage California to implement policies to increase retail demand responsiveness to price.

- The Commission can stimulate more demand response for the wholesale market by requiring CAISO to allow scheduling coordinators to bid load responses in the ancillary services market.⁴

- FERC Orders Addressing Supply-Demand Imbalance In The New York ISO Markets: FERC’s November 21, 2000 Order in New York Independent System Operator, 93 FERC ¶ 61,189 and its prior order in the same proceeding (93 FERC 61,073) emphasize the importance of demand response programs in the New York markets.

- FERC Staff Report On Midwest Markets: FERC’s Staff Report on “The Causes of Wholesale Electric Pricing Abnormalities in the Midwest During June 1998,” states that “retail customers had no incentive to adjust their usage based on price contributed to the price spike. Retail competition, coupled with the ability to respond in real time, could allow customers to see the price of the power they use and react accordingly. . . . These initiatives would help reduce the amount of power utilities would need to purchase on those days and would allow greater choice for customers.” FERC Staff Report, September 22, 1998, Chapter 4, Section A-6, page 4-6.

D. Appropriate Design Of A Market for Customer Load Response (CLR) Services

There are two distinct forms of demand responsive load service, one modeled after traditional state conservation and DSM programs, and a second that emphasizes active participation by customers and responsive load in power system and market operations. Though conservation and energy efficiency efforts remain important, the focus of the proposed CLR, RTO Function 9, is on the second type – active participation by responsive load in system and

⁴ Id. Chapter 6, Section 3, page 6-7, 6-9.

market operations. Industrial Consumers propose to call this new service Curtailable Load Response or CLR service.

RTOs should be required to facilitate the integration of CLR service into system and market operations commensurate with the manner in which ISOs currently integrate generation resources under Function 4. RTO facilitation of this market service will allow customers the flexibility to decide whether or not to participate, similar to existing generator participation in balancing and congestion management markets.

Like RTO Functions 1 through 7, Function 9 would depend on successful implementation of Function 8, “Interregional Coordination,” to establish reasonable consistency in the manner in which CLR markets operate across and among different RTOs. CLR should not be an RTO administered program as the traditional conservation or DSM programs were, but should be explicitly facilitated and administered by an RTO in the same manner that balancing and congestion management systems are administered by RTOs in tandem with RTO’s ancillary services responsibilities under Order 2000.

Industrial Consumers believe that FERC must jump start the demand response process. PennFuture, a group founded by former Pennsylvania Commissioner John Hangar, has issued a report that describes the current impasse in addressing demand response issues in Pennsylvania, a state most often touted for its successful retail access initiatives. “Breaking the Stick,” March 15, 2001, PennFuture Facts (available on web at PennFuture.org). The Report outlines the huge benefits to the public that demand response would bring, yet, as the summer of 2001 approaches, the talks drag on between the utilities (“Load Serving Entities”), PJM and the

Pennsylvania Public Utilities Commission without constructive resolution. FERC leadership is urgently needed.

In the March 14 Order, FERC recognizes that while states have jurisdiction over retail service, all weapons in FERC's arsenal have to be utilized to make markets operate more efficiently. Commercial transactions involving electricity must not be restricted from promoting productive and allocative efficiencies simply to preserve jurisdiction over such transactions. The industry has only two viable options for integrating demand (retail) and supply (wholesale) in a truly competitive electricity market. One is to let the states attempt to take charge. That would require them to overreach their jurisdiction and interfere with interstate markets for transmission and ancillary services. The other is for FERC to take charge consistent with state law. Certainly, if a state has opened its retail markets to competition, any retail customer should be deemed eligible to choose both from whom to buy as well as to whom to sell or resell load. In essence, FERC would be providing the wholesale market interface and wherewithal that retail customers need to exercise those freedoms. Thus it is not an intrusion on state jurisdiction. Industrial Consumers believe that by demonstrating the viability and benefits of this type of market in "open" states first, "closed" states will more readily initiate the restructuring of their jurisdictional utilities.

If one limits the program to "open" states, one cuts off considerable supply, certainly in the West. Since the serving utilities operate in the wholesale market, FERC should have influence over the participation in the wholesale market of Curtailable Load Response. States should be encouraged to cooperate.

E. Recommended FERC Action

The initial failure to include meaningful mechanisms for demand response in the emerging electricity markets is a significant oversight on the part of market designers – a market cannot function without a demand curve. In order to achieve participation by customers price-responsive load in electricity markets, Industrial Consumers propose that FERC conduct a technical conference to address CLR as a new RTO function. The technical conference should explore necessary certification procedures for participating suppliers of CLR services and procedures for the measurement and verification of “delivery” of CLR services.

FERC’s ultimate objective would be to:

- Require RTOs to provide a ninth minimum function, Function 9: Customer Load Response, which will specifically direct RTOs to remove all barriers to fully integrating price-responsive load into system operations and all RTO administered markets, including those for day-ahead energy, hour-ahead energy, balancing, and congestion management.
- Require all market operators to establish rules that allow price-responsive load to be offered into the markets on terms equal or comparable to those of generators.
- Revise the *pro forma* open access transmission tariff to explicitly integrate participation from price-responsive load. Require RTOs and all transmission providers to adopt new language in their *pro forma* open access tariffs that explicitly incorporates CLR in the following ancillary services. The appendix to Industrial Consumers’ Comments contains a red-

lined version of Ancillary Services requirements in the *pro forma* open access tariffs with illustrative changes for integrating CLR into the tariff.

- Adapt open access tariffs to facilitate the integration of CLR into regional markets and system operations.
- Require RTOs to explain how CLR will be integrated into balancing and congestion management markets at the same time that they file plans for these markets at FERC.

All market operators should be required to offer CLR in the fashion described or equivalent. CLR is not just a “today” or “day ahead” market. Many industrial customers can see weeks or months ahead and would be willing to reduce load for a defined period in exchange for a defined market based benefit.

F. Stakeholder Collaboration

A technical conference would be an ideal vehicle to encourage stakeholder collaboration to further the development and implementation of Function 9. Various stakeholder groups should be called upon to take actions necessary to implement CLR. The on-going efforts to develop these services in New York, California, and elsewhere would be appropriately reviewed and considered.

Industrial (and Other Participating) Consumers must:

- Work with RTOs to define the certification process that will establish the technical standards required for customer and load participation in energy and ancillary services markets.

- At their expense, install technologies for metering and communications.

We note that not all customers may need to install new metering and communications technology. There are some customers who undoubtedly already have an adequate level of technology that might be usable in summer 2001.

- Agree to standardized, consistent approach throughout the country to minimize overhead costs.

Transmission owners must:

- Install new technologies for communications and metering at customer sites.
- Work with energy customers to establish equitable rate schedules for payments and charges to customers that provide CLR.

RTOs (including independent entities that perform these functions for an RTO) must:

- Adopt consistent market rules to facilitate the integration of CLR into regional markets and allow customers with price-responsive loads to enter the markets as loads and to bid as loads, rather than requiring them to pretend to be generators .

III. INDUSTRIAL CONSUMERS' COMMENTS ON OTHER PROPOSALS RAISED BY FERC

Industrial Consumers support various aspects of FERC's March 14, 2001 Order, including: FERC's extension of waivers for QFs to increase generation by suspending temporarily operating and efficiency standards, the streamlining of regulatory procedures to

accommodate wholesale sales from on-site generation (including backup generators) and the authorization of market-based rates for such sales, and a proposal for FERC to order the interconnection of new generators with the grid if existing “impediments” prevent the generating resources from reaching load.

A. Industrial Consumers Also Encourage The Commission To Continue To Insist On A Single Western RTO

FERC recognized the urgent need for an end to California isolationism in its November 1, 2000 Order in San Diego Gas & Elec.:

California is physically integrated into an extensive interstate transmission grid and has therefore been part of a western electricity market for a long time. California’s markets will never realize optimal performance until the impediments to efficient utilization of the regional transmission grid are eliminated and the regional interstate transmission system is designed in such a way that it supports transparent, competitive Western bulk power markets -- markets that support all of the wholesale products that California requires, markets that remove impediments to efficient imports and exports, markets that eliminate rate pancaking and allow California to access more distant markets at a lower cost, markets that undertake regional transmission planning to ensure that the needs of California are considered when transmission expansions in other states are considered, and markets that allow regional market hubs like Palo Verde to develop where new generation can be located to serve multi-state markets. The Commission's RTO initiative is a response to fundamental changes in the electricity industry over the last 20 years. When fully implemented, RTOs will provide for operation and planning that will ensure consumer benefits for Californians and the citizens of other Western states. The problems being confronted in California can, in many ways, be traced to the continued balkanization of the Western grid and the absence of a true RTO with regional scope. The actions we have taken in this order are fully consistent with Order No. 2000, and nothing in this order relieves the ISO, PG&E, SoCal Edison or SDG&E from their obligation to make a filing in compliance with Order No. 2000 on January 17, 2001. We expect that the matters addressed in this order will move the California market toward meeting the significant objectives of Order No. 2000 and that these long-term market reforms will facilitate California’s transformation into a properly sized and functioning RTO.

CAISO's January 16, 2001 Order 2000 "Compliance Filing" was an example of an oxymoron: a blatantly non-compliant compliance filing. Industrial Consumers filed a brief comment in Docket RT01-85-000, urging that FERC impose a specific deadline on California to join DesertStar and RTO West.

On March 9, 2001, CAISO filed a response to numerous parties who protested CAISO's perfunctory January 16, 2001 filing. It is outrageous that CAISO continues its intransigence without any acknowledgment of the factors that FERC set forth in Order 2000 to assess adequacy of scope and configuration. CAISO states that since RTO West and DesertStar do not "yet exist, there is nothing for the CAISO to join." Like Southern Companies, CAISO insists that the RTO process is "voluntary" thereby seeking to evade the requirements of Order 2000. Such posturing mocks the Order 2000 filing requirements.

CAISO has been totally non-compliant with Order 2000. The problems that California is experiencing does not provide CAISO with a pretext to delay forming a westwide RTO; to the contrary, these problems require immediate westwide solutions. Any RTO of lesser dimension than the western interconnection would fall short of the minimum "scope and configuration" criteria.

B. FERC Should Exercise Its Authority Under Section 201(d)
Of The FPA To Facilitate Standard Interconnection Policies

At a December 9, 2000 hearing on the crisis in California markets (available on FERC web site), the Commissioners heard persuasive testimony from Calpine about the problem of inconsistent interconnection policies in California and other Western states. Mr. Macusi vividly described the differences in transmission policy, which delay interconnections, and the absence of standard, transparent and consistent procedures. The problem of delays in

interconnection is certainly not limited to California. FERC Staff's November 1, 2000 Report on the Midwest bulk power markets describes in graphic detail the games that are played that delay interconnection requests for months and years.

Industrial Consumers generally support the initiative by the Electric Power Supply Association (EPSA) to establish a model interconnection agreement to provide a framework for negotiations. As a precondition to developing new generating procedures, it is self-evident that developers in California, and other Western states, need a clear set of rules and procedures to govern requests and an assurance that their requests will be processed in timely and non-discriminatory fashion.

C. The Commission Should Extend And Broaden The Waivers Of Operating And Efficiency Standards, And Fuel Use Requirements For Qualifying Facilities

On December 8, 2000, FERC issued an order granting emergency waiver of certain regulations applying to PURPA Qualifying Facilities (QFs) to increase the available electric production from those plants.⁵ The Order cited approximately 9,000 MWs of QF capacity in California, with between 4,000 and 5,500 MW from qualifying cogeneration facilities. One party estimated that limited waivers would release as much as 1,000 MWs of additional capacity into the market for a limited time period.

In the March 14 Order the Commission is extending the temporary waivers to December 31, 2001. The waivers include:

- (1) Exemption from operating and efficiency standards for qualifying cogeneration facilities by allowing the owners or operators of the plant to sell

⁵ Docket Nos. EL00-95-000 & EL00-98-000.

their output above the level at which they have historically supplied this output to the purchasing utility. A plant's seasonal average output during the two most recent years of operation will define its historical output. FERC will require that all additional output from the cogenerators be sold exclusively through a negotiated bilateral agreement at market-based rates.

- (2) Exemption from fuel use requirements for qualifying small power production facilities (under Section 292.204(b)). The small power QFs also will be required to sell their excess production through negotiated bilateral contracts.

Industrial Consumers strongly support the extension of these waivers and urge the Commission to consider extending these waivers throughout the country for the pending summer peaking season.

Not all cogenerators sell their output. QFs should be able to use output for themselves to reduce other purchases. In normal times, a cogenerator should be able to make all the power it wishes while conforming to PURPA standards. In abnormal times such as the present, FERC may wish to consider the advisability of relieving restrictions on power sold by QF generators and small producers.

D. Additional Capacity from On-site Generation

In order to facilitate the use of existing on-site generation to meet demand, the Commission has adopted a streamlined regulatory procedure to accommodate wholesale sales from such facilities that will serve load within the WSCC. Beginning with the issuance of the Order, owners of generating facilities located within the Western Interconnection and used

primarily for back-up or self-generation, who would become subject to the Federal Power Act by virtue of sales of power from such facilities, will be permitted to sell power at wholesale from such facilities to non-affiliated entities without prior notice under section 205 of the FPA. FERC also authorizes such sales at market-based rates. The wholesale purchasers of such power sales will retain a burden to report such sales to the Commission on a quarterly basis.

Industrial Consumers strongly support this measure and urge the Commission to extend the applicability of it to other parts of the country for the pending summer peaking season. FERC may also wish to consider a short-term waiver for QFs to temporarily install non-QF generation and sell power without losing QF status.

E. Incentives For Electric Transmission Infrastructure

The Commission is proposing to provide incentives for the construction of new or enhanced transmission facilities in the West that will increase transmission capacity. For example, FERC proposes to allow cost-based rates reflecting a 300 basis point premium on equity and a 10-year depreciable life for facilities that are in service by July 1, 2001. A 200 basis point premium and 10-year depreciable life would be applied to facilities in service by November 1, 2001. A 100 basis point premium and 15-year depreciable life will be awarded to system upgrades (involving new rights of way and that add significant new transfer capability) in service by November 1, 2002. The Commission also proposes to award the construction of new transmission interconnection facilities that allow new generation to enter the market a premium of 200 basis points if in service by November 1, 2001 and 100 basis points if in service by November 1, 2002, provided that in either case, the construction accommodates the in-service date of the new generator. Finally, to the extent that transmission owners can increase transfer

capability on constrained facilities without significant capital investment (e.g., with improved operating practices or other technology-based applications), the Commission proposes to allow the owners to increase the revenue requirement of their network service rates to ensure that each additional MW of capacity will generate revenues equal to the provider's current firm point-to-point rate.

The Commission further assumes that a uniform baseline cost of equity of 11.5% for all transmission providers in the Western Interconnection. Thus, a premium of 300 basis points would result in a 14.5% effective return on equity.

The Commission assumed that many facilities that might qualify for these incentives are already underway or may not require initial siting and acquisition of rights of way, and has directed the CAISO and the transmission owners of the WSCC to file a list of potential candidates for such incentives.

Industrial Consumers are mindful of the serious need for new transmission capacity in the West and elsewhere. We are not convinced that the main impediment to getting new or enhanced facilities results from the lack of adequate return on the investment. The problems of some transmission "bottlenecks" are widely reported in the press and it is clear that other issues are at play and simply throwing easy money at the problem will not solve it.

Transmission owners are monopolists and any monopolist's natural behavior is to withhold supply (or service quality) to seek a higher price. We believe transmission owners are engaging in this behavior. In addition, many transmission systems are owned by utilities that are currently subject to retail rate freeze. This does create a legitimate problem that NEW investments cannot immediately be recovered in retail rates. But many, if not most of those

utilities asked for the rate freeze as part of a settlement process involving other issues such as stranded costs, provider of last resort, and the timetable for phasing in retail choice. Seeking a rate freeze or cap was their business decision. It is disingenuous of them to seek from FERC any form of waiver from such settlements under the guise of “incentives.”

The solution to both problems is to allow other entities (private or public) to bid for the rights to build or upgrade transmission facilities. The incumbent owners should not be entitled to a “franchise” on transmission services. The Commission is urged to reject the application of such incentives, as a matter of policy, because we believe it has only encouraged utilities to further stall or delay the necessary improvement to our Nation’s electric infrastructure.

Respectfully submitted,

[Signed]

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Dated: March 30, 2001

DESCRIPTION OF INTERVENORS

The Electricity Consumers Resource Council (ELCON) is an association of industrial consumers of electricity organized to promote the development of coordinated and rational federal and state policies that will assure an adequate, reliable and efficient electricity supply for all users at competitive rates. ELCON member companies produce a wide range of products, including: steel, aluminum, chemicals, petroleum, motor vehicles, industrial gases, machinery, glass, agricultural and food products, computer chips, paper and electronics. The member companies of ELCON consume approximately five percent of all electricity in the United States.

The American Iron and Steel Institute (AISI) is the principal trade association of the North American steel industry. Its member companies account for about seventy percent of the raw steel production in the United States. The steel industry is one of the most energy-intensive sectors in the United States; the cost of electricity for AISI members may constitute as much as twenty percent of the manufacturing cost of a steel mill product.

The American Chemistry Council (ACC) is a nonprofit trade association whose member companies represent more than ninety percent of the productive capacity of basic industrial chemicals in the United States. The manufacturing processes of many ACC member companies are highly energy-intensive. In addition, the chemical industry uses a substantial amount of self-generated electricity. Total electricity used by the industry, purchased plus self-generated, represents approximately eighteen percent of industrial electricity consumption in the United States and approximately six percent of national electricity consumption.

The American Forest & Paper Association (AF&PA) is the trade association of the forest, pulp, paper, paperboard, and wood products industry in the United States. It represents member companies engaged in growing, harvesting, and processing wood and wood fiber, manufacturing pulp, paper, and paperboard products from both virgin and recycled fiber, and producing engineered and traditional wood products. AF&PA members include manufacturers of over 80 percent of the paper, wood, and forest products produced in the United States and the members include small non-industrial private landowners, large multiproduct producers, and family-run mills. As such, AF&PA is the leading voice of the forestry, wood, and paper industries in the United States. AF&PA's members are among the nation's largest consumers of electric power, purchasing over 82 billion kilowatt-hours of electricity annually nationwide.

NOTICES AND COMMUNICATIONS

Notices and communications should be addressed to:

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CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing Motion to Intervene and Comments of Industrial Consumers were today mailed to parties on the service list of this proceeding by U.S. mail, postage prepaid.

Dated at Washington, D.C., this 30th day of March, 2001.

[Signed]

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Appendix D

PRO FORMA OPEN ACCESS

TRANSMISSION TARIFF

I. COMMON SERVICE PROVISIONS

1 Definitions

2 Initial Allocation and Renewal Procedures

3 Ancillary Services

Ancillary Services are needed with transmission service to maintain reliability within and among the Control Areas affected by the transmission service. The Transmission Provider is required to provide (or offer to arrange with the local Control Area operator as discussed below), and the Transmission Customer is required to purchase, the following Ancillary Services (i) Scheduling, System Control and Dispatch, and (ii) Reactive Supply and Voltage Control from Generation Sources and responsive load.

The Transmission Provider is required to offer to provide (or offer to arrange with the local Control Area operator as discussed below) the following Ancillary Services only to the Transmission Customer serving load or supplying energy from within the Transmission Provider's Control Area (i) Regulation and Frequency Response, (ii) Energy Imbalance, (iii) Operating Reserve - Spinning, and (iv) Operating Reserve - Supplemental.

The Transmission Customer serving load or supplying energy from within the Transmission Provider's Control Area is

required to acquire these Ancillary Services, whether from the Transmission Provider, from a third party, or by self-supply.

The Transmission Customer may not decline the Transmission Provider's offer of Ancillary Services unless it demonstrates that it has acquired the Ancillary Services from another source. The Transmission Customer must list in its Application which Ancillary Services it will purchase from the Transmission Provider. The Transmission Provider must develop certification procedures, in collaboration with both generators and responsive load, to identify which participants are able to supply ancillary services. The certification procedures for generators and responsive load must be comparable and non-discriminatory, and must explicitly facilitate the participation of responsive load in the supply of ancillary services.

If the Transmission Provider is a public utility providing transmission service but is not a Control Area operator, it may be unable to provide some or all of the Ancillary Services. In this case, the Transmission Provider can fulfill its obligation to provide Ancillary Services by acting as the Transmission Customer's agent to secure these Ancillary Services from the Control Area operator, ensuring

that the control area operator procures these services in a comparable and non-discriminatory manner from responsive load and generators. The Transmission Customer may elect to (i) have the Transmission Provider act as its agent, (ii) secure the Ancillary Services directly from the Control Area operator, or (iii) secure the Ancillary Services (discussed in Schedules 3, 4, 5 and 6) from a third party or by self-supply when technically feasible.

The Transmission Provider shall specify the rate treatment and all related terms and conditions in the event of an unauthorized use of Ancillary Services by the Transmission Customer.

The specific Ancillary Services, prices and/or compensation methods are described on the Schedules that are attached to and made a part of the Tariff. If the Transmission Provider offers an affiliate a rate discount, or attributes a discounted Ancillary Service rate to its own transactions, the Transmission Provider must offer at the same time the same discounted Ancillary Service rate to all Eligible Customers. Information regarding any discounted Ancillary Service rates must be posted on the OASIS pursuant to Part 37 of the Commission's regulations. In addition,

discounts to non-affiliates must be offered in a not unduly discriminatory manner. Sections 3.1 through 3.6 below list the six Ancillary Services.

3.1 Scheduling, System Control and Dispatch Service:

The rates and/or methodology are described in Schedule 1.

3.2 Reactive Supply and Voltage Control from Generation

Sources and Responsive Load Service: The rates and/or methodology are described in Schedule 2.

3.3 Regulation and Frequency Response Service: Where

applicable the rates and/or methodology are described in Schedule 3.

3.4 Energy Imbalance Service: Where applicable the rates and/or methodology are described in Schedule 4.

3.5 Operating Reserve - Spinning Reserve Service: Where applicable the rates and/or methodology are described in Schedule 5.

3.6 Operating Reserve - Supplemental Reserve Service: Where applicable the rates and/or methodology are described in Schedule 6.

SCHEDULE 1

Scheduling, System Control and Dispatch Service

This service is required to schedule the movement of power through, out of, within, or into a Control Area. This service can be provided only by the operator of the Control Area in which the transmission facilities used for transmission service are located. Scheduling, System Control and Dispatch Service is to be provided directly by the Transmission Provider (if the Transmission Provider is the Control Area operator) or indirectly by the Transmission Provider making arrangements with the Control Area operator that performs this service for the Transmission Provider's Transmission System. The Transmission Customer must purchase this service from the Transmission Provider or the Control Area operator. The charges for Scheduling, System Control and Dispatch Service are to be based on the rates set forth below.

To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs

(Name of Transmission Provider) Open Access Transmission Tariff
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charged to the Transmission Provider by that Control Area
operator.

SCHEDULE 2

**Reactive Supply and Voltage Control from
Generation Sources and Responsive Load Service**

In order to maintain transmission voltages on the Transmission Provider's transmission facilities within acceptable limits, generation facilities and responsive load (in the Control Area where the Transmission Provider's transmission facilities are located) are operated to produce (or absorb) reactive power. Thus, Reactive Supply and Voltage Control from Generation Sources and Responsive Load Service must be provided for each transaction on the Transmission Provider's transmission facilities. The amount of Reactive Supply and Voltage Control from Generation Sources and Responsive Load Service that must be supplied with respect to the Transmission Customer's transaction will be determined based on the reactive power support necessary to maintain transmission voltages within limits that are generally accepted in the region and consistently adhered to by the Transmission Provider.

Reactive Supply and Voltage Control from Generation Sources and Responsive Load Service is to be provided directly

by the Transmission Provider (if the Transmission Provider is the Control Area operator) or indirectly by the Transmission Provider making arrangements with the Control Area operator that performs this service for the Transmission Provider's Transmission System. The Control Area operator must procure this service from both generators and responsive load in a comparable and non-discriminatory manner. The Transmission Customer must purchase this service from the Transmission Provider or the Control Area operator. The charges for such service will be based on the rates set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by the Control Area operator.

SCHEDULE 3

Regulation and Frequency Response Service

Regulation and Frequency Response Service is necessary to provide for the continuous balancing of resources (generation and interchange) with load and for maintaining scheduled Interconnection frequency at sixty cycles per second (60 Hz).

Regulation and Frequency Response Service is accomplished by committing on-line generation whose output is raised or lowered (predominantly through the use of automatic generating control equipment) or by calling on responsive load that has been certified as being able to provide frequency regulation as necessary to follow the moment-by-moment changes in load and generation. The obligation to maintain this balance between resources and load lies with the Transmission Provider (or the Control Area operator that performs this function for the Transmission Provider). The Transmission Provider or Control Area operator must procure this service from both generators and responsive load in a comparable and non-discriminatory manner. The Transmission Provider must offer this service when the transmission service is used to serve

load or supply energy from within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Regulation and Frequency Response Service obligation. The amount of and charges for Regulation and Frequency Response Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

SCHEDULE 4

Energy Imbalance Service

Energy Imbalance Service is provided when a difference occurs between the scheduled and the actual delivery of energy to a load or supply of energy from a generator located within a Control Area over a single hour. The Transmission Provider must offer this service when the transmission service is used to serve load or supply energy from within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Energy Imbalance Service obligation. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator. The Transmission Provider or Control Area operator must procure this service from both generators and responsive load in a comparable and non-discriminatory manner.

The Transmission Provider shall establish a deviation band of +/- 1.5 percent (with a minimum of 1 MW) of the

scheduled transaction to be applied hourly to any energy imbalance that occurs as a result of the Transmission Customer's scheduled transaction(s). Parties should attempt to eliminate energy imbalances within the limits of the deviation band within thirty (30) days or within such other reasonable period of time as is generally accepted in the region and consistently adhered to by the Transmission Provider. If an energy imbalance is not corrected within thirty (30) days or a reasonable period of time that is generally accepted in the region and consistently adhered to by the Transmission Provider, the Transmission Customer will compensate the Transmission Provider for such service. Energy imbalances outside the deviation band will be subject to charges to be specified by the Transmission Provider. The charges for Energy Imbalance Service are set forth below.

SCHEDULE 5

Operating Reserve - Spinning Reserve Service

Spinning Reserve Service is needed to serve load immediately in the event of a system contingency. Spinning Reserve Service may be provided by generating units that are on-line and loaded at less than maximum output, and includes distributed generation or other on-site industrial generation that has been certified by the RTO as capable to provide spinning reserve. The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Spinning Reserve Service obligation. The Transmission Provider or Control Area operator must procure this service from all generators in a comparable and non-discriminatory manner. The amount of and charges for Spinning Reserve Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of

(Name of Transmission Provider) Open Access Transmission Tariff
Original Sheet No. 14

the costs charged to the Transmission Provider by that Control
Area operator.

SCHEDULE 6

Operating Reserve - Supplemental Reserve Service

Supplemental Reserve Service is needed to serve load in the event of a system contingency; however, it is not available immediately to serve load but rather within a short period of time. Supplemental Reserve Service may be provided by generating units that are on-line but unloaded, by quick-start generation or by interruptible or responsive load. The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Supplemental Reserve Service obligation. The Transmission Provider or Control Area operator must procure this service from both generators and responsive load in a comparable and non-discriminatory manner. The amount of and charges for Supplemental Reserve Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-

through of the costs charged to the Transmission Provider by
that Control Area operator.

(Name of Transmission Provider) Open Access Transmission Tariff
Original Sheet No. 17