

should not allow NERC to operate as a stand-alone reliability standard-setting organization with the ability to impose unjust costs on commercial transactions. Unless there is a single standards process that addresses both reliability and commercial issues simultaneously, there will be continual bickering and arguments between NERC and NAESB that cannot be resolved by the two groups.

FERC approval of NERC to address “reliability” and NAESB to address “commercial” issues will increase, perhaps substantially, FERC’s work load. Inevitably, FERC will be called upon to resolve both turf battles and substantive disagreements. The requirement that FERC referee disputes between NERC and NAESB will stifle the development of competitive markets and drain FERC staff resources.

These ELCON comments set forth general criteria that we believe should apply to any standard-setting organization. These criteria are:

1. A single organization must address both reliability and commercial, as well as retail and wholesale issues. ELCON believes that reliability and commercial standards (both retail and wholesales standards and gas and electric standards) are inextricably linked and cannot be separated. Two organizations should not try to address joint issues. (At Page 7)

2. The process used to set any standard must be ANSI certified. The American National Standards Institute (ANSI) will not certify any process that is not truly fair, open, balanced and inclusive. (At Page 9)

3. A professional, technical standards-drafting staff is essential. Any “volunteer” process in the electric industry will be dominated by utilities, generators and marketers. (At Page 10)

4. The staff of the organization should report to an independent Board. The staff should not be subjected to split Boards. Segment Boards, by definition, will be split on controversial issues. (At page 10)

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. GISB’s \$5,000 fee precludes many from participating, raises concern about the “pay to vote” requirement, and does not raise adequate funds to allow a professional, technical staff and compensate independent Board members. NERC has not established an adequate funding mechanism. (At page 11)

6. Finally, end-use customers pay all of the bills. Thus, they should have a very significant proportion of the vote in any governance process. ELCON believes that the governance of any standard-setting organization should be equally divided between two “classes”: end-use customers (the demand-side or those that pay the bills) and all of those entities that comprise the supply-side (those that affect the level of the bills in one way or another). Without such a structure, the supply-side will always out-vote the demand-side. ELCON recognizes that this lack of balance is a major concern to FERC. In fact, FERC has insisted that no one “class” should dominate entities like ISOs. However, the supply side “class” is dominating ISO decision-making. Such a lack of balance, to ELCON, is the primary reason why adequate demand response mechanisms have not been implemented in existing ISOs and RTOs. Such a lack of balance should not be allowed in standard-setting organizations. (At page 12)

Finally, ELCON offers specific recommendations that, if implemented, would result in a single process to address both reliability and commercial (as well as wholesale and retail) electric issues. (Pages 14 – 17)

B. Background

1. FERC Order

FERC issued an Order on December 19, 2001 providing guidance on the formation of a standards development organization for the wholesale electric industry.² The Order clearly implies that FERC intended for the industry to establish a *single* standards development organization: The title of the Order specifies guidance on the formation of “a” standards-development organization. Paragraph two of the Order says that FERC “prefer[s]” that “...the industry development these business practice standards

² “Order Providing Guidance on the Formation of a Standards Development Organization for the Wholesale Electric Industry,” Docket No. RM01-12-000, 97 FERC ¶ 61,289.

and communication protocols by establishing a *single* consensus, industry-wide standards organization for the wholesale electric industry...” (emphasis added) FERC continues: “If the industry does not agree, by March 15, 2002, on a *single* standards organization, we will institute our own procedures either to choose *an organization* [singular] to develop such standards or to develop the standards ourselves.” (emphasis added)

2. NAESB Activities

The Gas Industry Standards Board (GISB) decided in December 2001 to change its name to the North American Energy Standards Board (NAESB). NAESB proposed “quadrants” (wholesale and retail, electric and gas), thus expanding from its prior focus only on wholesale gas. The Wholesale Electric Quadrant (WEQ) of NAESB is being established to develop wholesale business standards.

3. NERC Response

The North American Electric Reliability Council (NERC) has been criticized for a number of years for failing to appropriately recognize the commercial impacts of reliability standards. In response to this criticism, and the direct competition from GISB (now NAESB) proposing to enter the electric-standard setting arena, a NERC Task Force proposed the “Wholesale Electric Standards Model” (WESM) that recognized that reliability and commercial issues cannot be separated. The WESM would have NERC the single standard-setting organization for the wholesale electric industry. NERC Board, at its October 16, 2001, meeting, unanimously endorsed the concept behind the

WESM.³ In fact, the NERC Board specifically agreed to: “Take all necessary steps to become the single organization in North America to develop both reliability standards and wholesale electric business practice standards through a fair, open, balanced, and inclusive process, and to file such standards with FERC and appropriate government agencies in Canada.”⁴

Unfortunately, the NERC Board reversed its earlier actions at its February 20, 2002, meeting.⁵ Specifically, the NERC Board now says that it will: "continue to set, monitor, and enforce compliance with ... standards for the reliable operation and planning of interconnected grids throughout North America” and that it will: “work with other electric industry organizations to create a workable process to coordinate NERC’s reliability standards development with the development by others of wholesale electric business practice standards and communications protocols ...” NERC issued documents following that Board meeting that further state:

- “We believe there is a paramount public interest in a reliable bulk power system in North America.”
- “We believe that core reliability standards normally can be crafted to accommodate the needs of transparent, non-discriminatory markets, and that, in most cases, implementation of those standards can effectively and efficiently be accomplished through market-based solutions.” ... “However, if and when the Board of Trustees of NERC believes that a business practice standard could compromise or adversely affect the reliability of the bulk power system, we

³ NERC Board Resolution titled: “Resolution on the Role of NERC in Developing Market Interface or Commercial Practice Standards (Board Agenda Item 20), approved unanimously on October 16, 2001 in Vancouver, Canada.

⁴ Ibid.

⁵ NERC Board Resolution titled: “Resolution on Responsibility for Reliability Standards,” approved unanimously on February 20, 2002, in Scottsdale, Arizona.

believe that the public interest requires that NERC be in a position to serve as an effective guardian of reliability.”

- NERC also says that it will “...identif[y] a list of core reliability standards that it intends to develop.” Conflicts that cannot be resolved will be filed with the appropriate regulatory body.
- NERC has expressed its view that, in addition to developing core reliability standards necessary for reliability, it will also need to be able to create reliability standards that address “urgent” reliability needs.

Following NERC’s announcement that it would abandon to NAESB the task of developing commercial practices, NAESB and NERC seem to be poised to recommend a two-organization model that will attempt to decouple “core reliability standards” and “policy development.”

4. Joint Industry Negotiations

A formal series of meetings was launched in December 2001 to try to develop an industry consensus in response to the FERC December 19th Order. These meetings were very well attended by many entities. However, the views of end-use consumers were lost to the numerous thoughts and ideas from those from various components of the supply-side. ELCON participated in these meetings, as well as numerous other meetings within NERC, NAESB, and other forums. Unfortunately, a consensus that is satisfactory to ELCON could not be reached.⁶

⁶ ELCON’s concerns with the proposals relate to: (1) our firm belief that the proposed “coordination” between two, separate organizations simply will not work given NERC’s stated position that reliability must be able to “trump” commercial issues, (2) a failure to adequately propose a funding mechanism that provides for professional, technical drafting staff, (3) the lack of a truly independent Board, and (4) the lack of appropriate representation of the demand (consumer) side in the governance process. Each of these concerns is addressed in more detail later in these comments. Additionally, the proposed memorandum of Understanding simply does not contain the kind of detail that is necessary to assure coordination between the two, conflicting groups.

C. ELCON Comments

1. **A single organization must address both reliability and commercial, as well as retail and wholesale issues.** The initial reaction may be that NAESB has won the “competition” to be certified as a commercial practices organization and that NERC will only deal with a few, non-commercial standards. However, NERC believes it can (and will) develop not only the “core reliability standards” (whatever they include), but also any other reliability standards that address “urgent” reliability needs. NERC believes that it must be able to “trump” any commercial standard NERC believes will negatively impact reliability. Further, if the implementation of core reliability standards cannot be crafted to accommodate the needs of commercial markets, NERC seems to believe that the public interest requires NERC to prevail -- the standard will assure reliability no matter the commercial impact. It is easy to envision a recurrence of the type of disputes that arose when FERC initiated Policies 3 and 9—Tagging and Transmission Line Loading Relief (TLR).

The impact on FERC of two separate standard-setting processes will be as disadvantageous as the impact on the markets:

- ❑ Given that reliability and commercial standards (both retail and wholesale standards and gas and electric standards) are inextricably linked, there will be many areas of disagreement between the two separate organizations.
- ❑ No amount of “coordination” will eliminate the disagreements.
- ❑ Ultimately, the disagreements, and there will be many of them, will come to FERC for resolution.

On July 25, 2001, NERC's General Counsel David Cook testified before the Senate Energy Committee. His testimony was presented for the purposes of advocating legislation accrediting a North American Electric Reliability Organization. The testimony is of interest in a context for which it was not intended, which is a recognition of the inevitable interplay between reliability and commercial impacts. NERC notices first that the electric reliability regime that served the nation from the mid 1960's to the mid 1990's does not work well under the new regime:

- The grid is now being used in ways for which it was not designed.
- There has been a quantum leap in the number of hourly transactions, and in the complexity of those transactions.
- Transmission providers and other industry participants that formerly cooperated willingly are now competitors...
- The single, vertically integrated utility that formerly performed all reliability functions for an area is being disaggregated, meaning that reliability responsibilities are being divided among many participants.
- Some entities appear to be deriving economic benefit from bending or violating the reliability rules.
- Construction of additional transmission capacity has not kept pace with either the growth in demand or the construction of new generating capacity, meaning the existing grid is being used much more aggressively.

As a result of these factors, NERC observes that “the transmission grid is becoming increasingly stressed.” NERC describes the economic impact on the marketplace of transmission curtailments taken in the name of reliability:

... NERC is seeing more congestion on the grid, for more hours of the day. Last summer in the Eastern Interconnection there were substantial transfers of power from north to south. Cooler temperatures in the north meant that surplus generation could be sent to the south where the temperatures were hot and natural gas prices were high. On many days security coordinators had to

invoke NERC transmission loading relief procedures to curtail transactions that were overloading transmission facilities between north and south. For generation sellers, these curtailed transactions resulted in lost business. Buyers were forced to replace these transactions with higher priced power, or in some cases, to cut off power to certain “interruptible” customers. In addition, what do not show up are the transactions that merchants or marketers decided not to engage in because of the likelihood they would be interrupted. Today, we know that those same transmission facilities are fully subscribed for the coming summer, meaning we could see a repeat of last year’s pattern if we experience similar weather conditions and fuel prices.

The reality – or even the perception – that actions taken in the name of reliability have an anticompetitive motive damage the Commission’s goal of encouraging robust power markets.

Attempts to address reliability and commercial issues in separate organizations will necessarily result in continual disputes over jurisdiction, inter-relationships, priorities, etc. A single organization must address both reliability and commercial issues in both retail and wholesale markets. This organization – which would include both NERC and NAESB, albeit both significantly restructured – should establish uniform standards for North America.

2. The process used to set any standard must be ANSI certified. The process used by any standard-setting organization must be fair, open, balanced and inclusive. The American National Standards Institute (ANSI) will not certify any process unless it truly meets these criteria.

ELCON recognizes that GISB is ANSI certified and NAESB expects to have the same certification in the near term. However, NERC now proposes a process

that would allow the NERC Board to overturn any standard that has gone through the WESM process that, in the Board's view, negatively impinges on reliability. NERC has not even filed for ANSI certification. ELCON questions whether ANSI will certify a process that can be overturned by that organization's Board.

3. ELCON believes that a professional, technical standards-drafting staff is essential. An all-volunteer processes requires tremendous contributions of time from the members. Consumers, including industrial users, cannot devote enough staff time to adequately participate in an all "volunteer" process.

It is very important to recognize that "volunteers" actually are "biased participants." Individuals are paid to participate in the standard-setting organization. In nearly every case, they are expected to advocate policies and positions that benefit their employer. An all "volunteer" organization thus hears more from those market participants that have the greatest resources. Any "volunteer" process in the electric industry will be dominated by utilities, generators and marketers.

A professional, technical standards-drafting staff, operating under very clearly specified guidelines, can greatly enhance the abilities of resource-constrained parties to participate. NAESB does not have, nor does it propose to have, a professional, technical, standards-drafting staff. This is a major deficiency.

4. The staff of the organization should report to an independent Board. ELCON does not believe that sector or segment Boards deal well with policy or other difficult issues or interpretations. The problems of the California ISO Segment Board highlight these concerns. While we do not expect the Board of any standard-

setting organization to set policy, we do believe that there will be many instances where interpretations of policy must be made – interpretations regarding the reliability vs. commercial impacts are clear examples. The staff should not be subjected to split Boards any more than absolutely necessary. Segment Boards will be split on controversial issues. Thus, we believe the standard-setting organization should have an independent Board. NAESB has a segment Board. This 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. ELCON believes that a professional, technical standards-drafting staff is essential (Point #3 above) and that this staff should report to a truly independent Board (Point #4 above). Each of these attributes requires funds.

GISB funds its operations with a \$5,000 fee from each member. Only Members can serve on either the Executive Committee or the Board. Further, only members can vote in the final approval process for the standards. GISB can afford a staff of only three persons total with this funding mechanism. Further, many potential participants to the GISB/NAESB process have complained that the \$5,000 fee precludes them from participating and others are concerned about the “pay to vote” aspect.

A specific example highlights the concern that a \$5,000 fee precludes participation. GISB has been operating for a number of years. The GISB “End User” segment presently includes 19 Members. However, over half of these “end users” are electric utilities. There is only one end-user in the traditional sense (Boeing Co.). Two

others represent federal end-users (the Defense Energy Support Center and the U.S. Department of Energy). None of the rest are end-users.

NERC has been funded by the 10 Regional Reliability Councils (RRCs). This funding mechanism has allowed NERC to have a relatively large staff. However, this funding mechanism also has given undue influence to the RRCs and is the source of much concern and opposition.

ELCON believes that any standard-setting organization must have a funding mechanism that does not include a “pay to vote” requirement, yet develops enough money to pay for a professional, technical writing staff. If a membership fee is charged, it must not be so high as to restrict participation.

6. Finally, end-use customers pay all of the bills. Thus, they should have a very significant proportion of the vote in any governance process. ELCON members have experienced significant frustration over the experiences with other organizations – especially existing Independent System Operators (ISOs) – regarding the lack of sensitivity of the needs of end-use customers. ELCON Members believe strongly that the supply-side will always prevail when customers have only 20% (or even 25%) of the vote.

As an example, congestion can be relieved through one of at least three methods: increased transmission to mitigate the constraint, increased generation on the congested side of the constraint, or demand response. Unless there is equality of representation between the supply- and demand-sides, the choice will be resolved in favor of the interests of the supply-side.

More precisely, ELCON believes that the electric industry is actually composed of two very different “classes” of participants: those that receive electric bills and pay them and all of the others in the supply chain that affect the level of the bills. Attachment A to these comments explains these thoughts in more detail.

ELCON believes that the governance of any standard-setting organization should be equally divided between these two “classes”: end-use customers (the demand-side or those that pay the bills) and all of those entities that comprise the supply-side (those that affect the level of the bills in one way or another). Without such a balance, the supply-side will always out-vote the demand-side.

This lack of balance is a major concern to FERC. Specifically, FERC has insisted that no one class should dominate entities like ISOs. In fact, the supply side “class” is dominating ISO decision-making.

The lack of balance, to ELCON, is the primary reason why adequate demand response mechanisms have not been implemented in existing ISOs and RTOs. Until there is true parity between the demand- and supply-sides, such results will continue. Such a lack of balance should not be allowed in standard-setting organizations. Unfortunately, neither NERC nor NAESB are recommending governance structures that are even close to such a balance.

In sum, neither NERC nor NAESB comply with the general characteristics ELCON believes are essential. NERC has a professional, technical staff and an “independent” Board. However, NERC has chosen to give preference to reliability over commercial issues, is not ANSI certified, doesn’t have an adequate funding mechanism,

and proposes a segment structure that gives short shrift to end-use customers. NAESB is ANSI certified. However, NAESB limits its scope to commercial issues, does not have a professional, technical staff, has a segment Board, has a “pay to vote” funding mechanism that is restrictive to some stakeholders, and has a segment structure that gives short shrift to end-use customers.

D. ELCON Recommendations

ELCON urges FERC to give clear guidance to both NERC and NAESB that will result in compliance with both the letter and the spirit of FERC’s December 19th Order – that is, the creation of a *single* standard-setting process for the wholesale electric industry. Specifically, ELCON urges FERC to explicitly state that any standard that is filed with FERC for approval must be developed and approved in a single process that:

- ❑ Is ANSI-certified and gives equal recognition to both reliability and commercial considerations.
- ❑ Is “customer friendly.” This requires a professional, technical staff that provides assistance in both the drafting and editing aspects of standard-development.
- ❑ Is overseen by a truly independent, objective Board that will assure both compliance with the process. However, the Board must not be able to overturn any standard developed and approved in the ANSI-certified process.
- ❑ Assures a governance structure that gives equal recognition to both the demand and the supply segments.⁷

Such FERC guidance could result in a satisfactory “merging” of NERC and NAESB. NERC could “occupy” the Wholesale Electric Quadrant (WEQ) of

⁷ Specifically, a governance structure with only two segments: end-use customers (the demand-side) and all other stakeholders (the supply side).

NAESB.⁸ However, to do so, both NERC and NAESB must incorporate changes to their present proposed structures and procedures. ELCON's specific recommendations for FERC actions to achieve this "merger" are set forth below.

1. Required NERC Changes

ELCON filed comments with NERC prior to its February 20, 2002, Board meeting.⁹ In these comments, ELCON specifically urged NERC to take specific actions to enable NERC to "occupy" the WEQ. NERC chose not to make the changes. ELCON now urges FERC not to endorse NERC without the following changes:

- ❑ Remove the word "reliability" from its name. As long as the word reliability is in the name, there will be at least a perception that commercial issues not considered.
- ❑ Explicitly agree to give reliability and commercial issues equal treatment in all aspects of the standard-development process.¹⁰
- ❑ Explicitly commit to "occupying" the Wholesale Electric Quadrant (WEQ) of the North American Electric Standards Board (NAESB). This will require NERC to work with NAESB to achieve the necessary by-law and other changes required to have NERC occupy the WEQ.
- ❑ Explicitly state that all standards resulting from the process will be filed with the Federal Energy Regulatory Commission (FERC) [at least in the U.S.]. No standard should be enforceable prior to FERC approval.
- ❑ Commit to have a funding mechanism in place by the end of 2002 that will allow participation by all end-use customers without requiring prohibitive membership

⁸ In essence, NAESB could "subcontract" or "outsource" the wholesale electric quadrant to a revised and restructured NERC.

⁹ The ELCON comments are posted on both the ELCON and NERC web sites.

¹⁰ It is important to note that the current NERC Board has clearly stated that it does not intend to give equal treatment to reliability and commercial issues. Thus, the current NERC Board must make significant changes either in composition or in stated objectives to be able to function in the required manner.

fees. FERC should assure that the costs of the standard-setting organization are just and reasonable.

- ❑ Explicitly agree to immediately file with the American National Standards Institute (ANSI) for accreditation of the standards-setting process and, further, commit to making any changes to the WESM proposal necessary to achieve such accreditation.
- ❑ Finally, but of most importance, assure that end-use customers or their representatives have at least half of the total vote in the governance process.

2. Required NAESB Changes

NAESB will also have to make changes in its proposed structure and procedures. ELCON urges FERC not to endorse NAESB without first incorporating the following changes to its process and structure. Specifically, NAESB must allow:¹¹

- ❑ The WEQ to establish its own membership and funding criteria.
- ❑ NERC's Board to govern the WEQ standards development process (but not allow the NERC Board to vote on approval of standards as part of the standards process).
- ❑ Members of the NERC Board to serve as the WEQ representatives of the NAESB Board.
- ❑ The NERC Standards Authorization Committee to serve as the WEQ Executive Committee (except that it will not vote on the approval of standards).
- ❑ The WEQ to prioritize its own standards, and establish its own standards development plan, budget, and funding mechanism.
- ❑ NERC to participate in the NAESB Triage function to assure that standards affecting more than one quadrant are appropriately addressed.

¹¹ These specific points were developed by the NERC Standing Committees Representation Task Force. See: "Development Wholesale Electric Standards, Final Report to the NERC Stakeholders Committee and Board of Trustees, by the NERC Standing Committees Representation Task Force," February 7, 2002 at page 6. This document is contained in Agenda Item 11 of the NERC Board meeting of February 20, 2002, in Scottsdale, AZ.

By taking these specific actions, FERC will ensure a process that both assures the development of wholesale electric standards with equal treatment of reliability and commercial impacts and minimizes filings at FERC requesting adjudication of squabbles between two competing organizations.

Respectively submitted,

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Appendix A to the Comments of the Electricity Consumers Resource Council (ELCON) in FERC Docket No. RM01-12-000 Regarding:

“Under-representation Of End-use Customers in Governance”

The governance process in ISOs, RTOs and standard-setting organizations is seriously flawed. End-use customers who represent the demand-side of the market have no more than 25% (and often much less) of the vote in most ISO and RTO boards and stakeholder advisory committees. End-use customers are repeatedly and inevitably outvoted on programs of vital importance to all consumers, e.g., demand response and congestion management.

ELCON believes that the electric industry is actually composed of two very different “classes” of participants: those that receive electric bills and pay them and all of the others in the supply chain that affect the level of the bills. There must be an appropriate balance between the two classes.

FERC has commendably tackled many important principles related to RTO governance, e.g., passive ownership and limits on ownership by market participants. It is now urgent that FERC address an imbalance between end-use customers (the demand side) and supplier interests.

A. Nature Of The Problem

Existing ISOs, RTOs and standard-setting organizations have gerrymandered class structures which over-represent the generators, transmission and distribution companies and power marketers--the aggregate supplier class. End-use customer interests (including residential, commercial and industrial consumers; municipal, state and federal power purchasers; and other entities who actually pay electric bills) are inevitably outvoted on issues that pit supply-side solutions against demand-side solutions. All too often, interests of the demand- and the supply-side clash. In such cases, FERC should require balanced representation. This re-tooling of governance is necessary i) to assure independence; ii) to further FERC's core statutory mandate to protect consumer interests; and iii) to assure effectuation of key FERC policies such as implementation of optimal demand-response.

FERC has allowed each ISO and RTO to determine its own classes or categories of participation in stakeholder committees and stakeholder boards. It is typical for ISOs and RTOs to have 5 or 6 categories of market participants represented on boards and committees. Rather than prescribe specific "classes," FERC has let a thousand flowers bloom. FERC's initial test for balance of representation -- "No one class can veto a decision reached by the rest of the board and no two classes can force through a decision that it is opposed by the rest of the board" -- must be refined to assure that no one sector dominates because the concept of "class" has not been adequately defined.

FERC stated in Order 2000 that due to insufficient experience with the fledgling ISO and RTO concept, it was reluctant to specify too many details about governance.

With some experience under its belt, FERC can and should provide further prescriptive detail with respect to assuring balance in governance.

ELCON advocates a 50%-50% division of representation between those who supply and those who actually pay the electric bills. Unless there is equality of representation, decisions regarding issues such as how to relieve congestion will be biased. As an example, congestion can be relieved with either increased generation, increased transmission, or demand response. Without balance between the demand and supply interests, the decision will be resolved in favor of the interests of the supply-side.

B. Rationale For FERC Review Of ISO, RTO and Standard-setting Organization Governance

ELCON urges that FERC's review of this governance issue be guided by three fundamental questions: (i) Does under-representation of demand interests threaten the purpose of independence? (ii) Does FERC's statutory mandate require FERC attention to the problems of chronic under-representation of consumer interests? (iii) Does failure to equalize participation by the demand and supply interests threaten the achievement of FERC policy objectives?

- i) Does The Under-Representation Of Demand Interests Defeat The Purpose Of The Independence Requirement?

In Order 888, FERC first articulated its ISO Principles:

1. The ISO's governance should be structured in a fair and non-discriminatory manner.

The primary purpose of an ISO is to ensure fair and non-discriminatory access to transmission services and ancillary

services for all users of the system. As such, an ISO should be independent of any individual market participant or any one class of participants (e.g., transmission owners or end-users). A governance structure that includes fair representation of all types of users of the system would help ensure that the ISO formulates policies, operates the system, and resolves disputes in a fair and non-discriminatory manner. The ISO's rules of governance, however, should prevent control, and appearance of control, of decision-making by any class of participants.

75 FERC ¶ 61,080 (1996). See also Atlantic City Electric Co., 77 FERC ¶ 61,148 (1996). This ISO principle was codified in Order 2000 at 18 C.F.R. (j)(ii) (“The RTO must have a decision-making process that is independent of control by any market participant or class of participants.”). As FERC stated in the RTO NOPR, Docket RM99-2, RTO decision-making should not be controlled by any one class of participants:¹²

Market participants must be assured that the RTO will provide transmission access to all market participants on a fair and non-discriminatory basis. The Commission believes that it is a prerequisite for achieving fair, open and competitive power markets. An RTO needs to be independent in both reality and perception. As we have said before in the context of ISOs, we think that “the principle of independence is the bedrock upon which the ISO must be built...” It is the Commission's view that independence can be achieved if the RTO satisfies three conditions. First, the RTO, its non-stakeholder governing board members and its employees must have no financial interests in market participants. Second, the RTO's decision making must not be controlled by any market participants. Third, the RTO must have independent authority to file changes to its transmission tariff.

¹² The same conclusion was reached by the DOE Reliability Task Force and the NERC Reliability Panel. The DOE Task Force concluded that regional reliability entities must be “truly independent of commercial interests so that their reliability actions are--and are seen to be--unbiased and untainted...” Task Force Report at xv. The Electric Reliability Panel concluded that “(t)o dispel suspicions that the system operator favors one participant over another... the operator must be independent from market participants.” North American Electric Reliability Council, Electric Reliability Panel, Reliability Power: Renewing the North American Electric Reliability Oversight System, December 22, 1997, at 17.

Dominance by the supply-side defeats the key governance objective that no one segment of the industry should dominate ISO and RTO decision-making:

An ISO governing board's delegation of decisions to a stakeholder committee would be contingent on this committee not being dominated by one segment of the industry. We recently found that the existing tiered governance arrangements of the New York and New England ISOs failed to meet this standard and we ordered both ISOs to reduce the voting power of dominant utilities in the lower tier of stakeholders charged with advising the non-stakeholder governing boards. See Central Hudson, 87 FERC ¶ 61,135 (1999); New England Power Pool, 86 FERC ¶ 61,262 at 61,965.

Docket RM99-2, 87 FERC ¶ 67,173 (1999) fn. 190.

FERC should adopt safeguards to assure that the supply-side does not use its overwhelming voting power to operate ISOs, RTOs and standard-setting organizations in a way that serves supply-side interests to the detriment of the public good. By analogy, in Order 2000, FERC addressed concerns that passive ownership interests “be truly passive and in no way interfere with the independent operation and decision making of the RTO.” FERC sought to address concerns that passive ownership would allow existing transmission owners to continue to control use of transmission assets and ultimately deny equal access to competitors. Accordingly, FERC established a compliance audit function. Similar safeguards are needed to preserve ISO, RTO and standard-setting organization balance and independence by assuring that suppliers do not overwhelm customers interests.

ii) Is Under-Representation Of Demand Interests Consistent With Statutory Duty To Protect Consumers From Exercise Of Monopoly Power?

FERC's "primary aim" is "to protect consumers against exploitation" at the hands of monopolist utilities. Process Gas Consum. v. FERC, 177 F.3d 995, 1002 (D.C. 1999). See FPC v. Hope Natural Gas Co., 320 U.S. 591, 610 (1944); see also Public Sys. v. FERC, 606 F.2d 973, 979 n.27 (D.C. Cir. 1979) ("control of the economic power of utilities that enjoy monopoly status' is the focus of regulation under the Natural Gas Act and the Federal Power Act"). See City of Detroit v. FPC, 230 F.2d 810 (D.C. 1955), where the court found that the Commission's approach to incentive pricing could not be squared with the Federal Power Act:

While as we have indicated the Commission may be empowered to consider some of these factors it must also, and always, relate its action to the primary aim of the Act to guard the consumer against excessive rates.

230 F.2d at 817. The Federal Power Act's "primary orientation . . . toward the maintenance of low prices for the consumer" (230 F.2d at 818) precludes the Commission from authorizing ISOs, RTOs and standard-setting organizations which may impose higher rates on consumers than necessary due to an unbalanced governance structure.

ELCON is a strong proponent of Order 2000. FERC must assure, however, that RTOs'/ISOs' exercise of transmission authority does not result in unreasonable rates to consumers or discrimination. While ISOs, RTOs and standard-setting organizations are intended to foster light-handed regulation, FERC cannot abdicate its statutory duty under

FPA § 205 and § 206.¹³ While concededly, FERC can review complaints related to ISOs, RTOs and standard-setting organizations governance, FERC will be deluged with complaints if it does not insist that ISOs, RTOs and standard-setting organizations adopt and implement open and balanced governance structures. e.g., Cargill-Alliant, 98 FERC ¶ 61,148 (2002).

FERC should solicit comments in its SMD NOPR on the extent to which ISOs, RTOs and standard-setting organizations governance structures have in effect disenfranchised consumer interests by locking consumer interests into such a small percentage of voting participation that Industrial Consumers, residentials, and other customers are inevitably outvoted each time a topic is considered that pits demand interests against supply interests. By inviting comments on experience to date with ISOs, RTOs and standard-setting organizations governance, FERC will build a record adequate to sustain its final rule on standard market design.

¹³ The Commission is granted the authority and responsibility by FPA sections 205 and 206, 16 U.S.C. §§ 824d, 824e, to ensure that the rates, charges, classifications, and service of public utilities (and any rule, regulation, practice, or contract affecting any of these) are just and reasonable and not unduly discriminatory, and remedy undue discrimination in the provision of such services. The Commission is required to address, and has the authority to remedy, undue discrimination and anticompetitive effects. The Commission has a statutory mandate under these sections to ensure that transmission in interstate commerce and rates, contracts, and practices affecting transmission services, do not reflect an undue preference or advantage (or undue prejudice or disadvantage) and are just, reasonable, and not unduly discriminatory or preferential.* The Commission’s regulatory authority under the FPA “clearly carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of interstate utility operations pursuant to [FPA] §§ 202 and 203, and under like directives contained in §§ 205, 206, and 207.”**

* Once such a finding is made, the Commission is required to remedy it. See, e.g., Southern California Edison Company, 40 FERC ¶ 61,275 at 61,873 (1990), modified sub nom., Cities of Anaheim v. FERC, 941 F.2d 1234 (D.C. Cir. 1991); Delmarva Power and Light Company, 24 FERC ¶ 61,199 at 61,466, order on reh’g, 24 FERC ¶ 61,380 (1983).

** Gulf States Utilities Co. v. FPC, 411 U.S. 747, 758-59, reh’g denied, 412 U.S. 944 (1973).

iii) Does The Under-Representation Of Demand Interests Jeopardize FERC Policy Objectives On Demand-Response?

FERC's policy objectives cannot be achieved in an environment where supply-side interests dominate ISOs, RTOs and standard-setting organizations decision-making with respect to the conflict between supply-side and demand-supply solutions.

On December 17, 2001, FERC issued an excellent Discussion Paper of its "Vision of the Future" to facilitate discussion of RTO policy regarding standard market design. Industrial Consumers submit that key aspects of FERC's Vision will be frustrated if the demand-side continues to be under-represented. For example, the Vision Statement calls for a world where "Buyers will receive accurate and timely price signals and will have the ability to react to them, so that they can make rational and efficient choices in the amount of energy they consume at any given point in time. As a result, demand will be responsive to price changes." FERC's February 7, 2002 Strawman for Market Power and Mitigation states that "If and when a region develops substantial price-responsive demand, there will be less of a need for mitigation rules...."

In its 2001 Report "Competition and Consumer Protection Perspectives on Electric Power Regulatory Reform," the FTC identified three key advantages of demand-response: Enforced demand-response (i) can be expected to "moderate wholesale spot market prices and price volatility;" (ii) "improve reliability for electricity;" and (iii) "moderate market power." FTC notes that price responsive demand can reduce the profitability of economic withholding in wholesale spot markets.¹⁴

¹⁴ The FTC states:

While in most ISOs, RTOs and standard-setting organizations, generators and other supply-side interests pay lip service to supporting demand-response programs, efforts to adopt adequate demand-side measures are being opposed by supply-side interests that benefit from inflexible demand. Because the governance structure of ISOs, RTOs and standard-setting organizations does not contain sufficient representation of the demand-side, sub-optimal policies result.

Large retail customer participation in wholesale markets, coupled with variable retail pricing, would benefit all retail customers, because the average price paid by all customers decreases as peak demand is reduced. These programs increase system reliability, mitigate the potential for price spikes during periods of peak demand and supply scarcity, and increase the opportunity for retail suppliers to add value to commodity reselling, as well as indirectly reduce the environmental impacts of electricity production. Moreover, real-time, demand-side participation by wholesale buyers and large retail customers of electricity can potentially mitigate existing electricity supplier market power and increase incentives to attract customers by lowering prices.