TESTIMONY OF JOHN ANDERSON, EXECUTIVE DIRECTOR OF THE ELECTRICITY CONSUMERS RESOURCE COUNCIL (ELCON), BEFORE THE SENATE COMMITTEE ON ENERGY AND NATURAL RESOURCES, MARCH 27, 2003

SUMMARY OF TESTIMONY BY JOHN ANDERSON BEFORE THE SENATE COMMITTEE ON ENERGY AND NATURAL RESOURCES, MARCH 27, 2003

ELCON is the national association representing large industrial users of electricity. ELCON members seek competitive wholesale and retail competitive markets. ELCON supports including electricity provisions in a comprehensive energy bill only if such provisions clearly will advance the cause of competitive markets.

- **Regional Energy Services Commission:** This proposal is untested and could hinder, not facilitate, the flow of power.

- **Reliability Standards:** The "consensus" legislation could balkanize the market (by granting deference, or providing a rebuttable presumption to certain groups); it also does not take into account the intrinsic inter-relationship between reliability standards and their commercial impact.

- **Open Access (FERC-Lite):** Optimally, at some point, the entire grid, regardless of ownership, will be open and subject to uniform rules and regulations.

- **Transmission Siting:** Granting FERC a "fallback" right of eminent domain, as provided in the House draft, while rarely used, would provide a motivation to ensure that state inaction does not occur.

- **Transmission Investment Incentives:** Investment incentives will be costly to consumers. Investment incentives can already be offered by FERC on a case-by-case basis; there is no demonstrated need to utilize investment incentives in all instances.

- **Transmission Cost Allocation (Participant Funding):** This should be considered as a regulatory issues, not a legislative one. Under current law, FERC can allocate the cost of new transmission in any way it deems appropriate – one approach, i.e., participant funding, should not be locked into statute.

- **Transmission Organizations/RTOs:** ELCON supports large RTOs with independent governance; legislation is not needed on this issue.

- **PUHCA:** Given recent turmoil in electricity markets, repeal of PUHCA – which protects both consumers and investors – seems unwise.

- **PURPA:** PURPA guarantees to cogenerators regarding purchase of electricity and the availability of back-up power should be retained until functioning competitive markets are established.

- **Net Metering and Real-Time Pricing:** ELCON members support the concept of net metering; if real-time pricing is required, a utility's risk is reduced and, we believe, its potential rate of return should be reduced as well.

- **Market Transparency, Anti-Manipulation, Enforcement:** The suggested language seems minimal considering the abuses that have been revealed in electricity markets.

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Good morning. My name is John Anderson. I am the executive director of the Electricity Consumers Resource Council, or ELCON. ELCON was established in 1976 and is the national association of large industrial consumers of electricity. Our members come from virtually every segment of the manufacturing community and have operations in every state.

ELCON members compete in free and open markets here in the U.S. and abroad. We support competition, and, accordingly, for over ten years, ELCON and ELCON members have sought free and open electricity markets at the wholesale and retail levels. We have testified to that purpose before this Committee on several occasions.

At present we find that progress toward competition is being made – slow progress to be sure, but progress nevertheless. At the wholesale level especially, more power is being bought and sold than ever before. There are independent generators, marketers and other participants trading electricity that we believe is beneficial to all consumers, industrial, commercial and residential.

The evolution to a truly competitive wholesale market is far from complete. That market is very much in transition. It is changing partially in response to the pro-competition directives of the Energy Policy Act of 1992 and from FERC, specifically Orders 888 and 2000, and partially in response to market developments.

I hasten to add that, regarding wholesale markets, progress must be made at the national, rather than state or regional, level. Our grid is interconnected; electrons cross state and regional boundaries with impunity. The Federal Energy Regulatory Commission (FERC) is the plenary regulatory body with the statutory authority necessary to deal with interstate electricity issues. Last year's Supreme Court case affirmed FERC's jurisdiction over interstate transmission. We urge Congress and this Committee not to tamper or try to modify the basic holdings of that decision.

Before I address the individual issues before this Committee, I would like to state that while we as industrial consumers do not oppose the eventual enactment of an electricity title, we do not encourage one either. Markets are rapidly evolving. Participants are aware of the rules and are responding to market forces. Legislation is not necessary at this point in time.

My fear, and I have observed this in several states that adopted so-called electricity restructuring plans, is that legislative solutions, almost by necessity, involve political compromises. And too often those compromises create costly market problems without providing market solutions.

So if this Committee is certain that it is crafting legislation that will make markets more competitive, that will remove the barriers that monopoly utilities have hidden behind for decades, and will provide more options and lower prices for consumers, I say go ahead and ELCON will support you.

But if instead you are drafting legislation that you hope addresses one company's problems, one region's uniqueness, or one Senator's political needs, I urge you to go slow. In fact, unless we are sure of what will, in fact, make electricity markets more competitive, I would urge the Committee to take no action on electricity at this time.

I will now elaborate on the various sub-issues that are part of the legislative proposals before the Committee today. Given the complexity of each issue, I have tried to state our objectives somewhat simply. In all cases, we are striving for more competitive markets.

Regional Energy Services Commission (RESCs)

From a personal perspective, let me say that I have worked on electricity policy issues for over twenty-five years. Although some claim that the issues rarely change, every now and then there emerges a completely new proposal. Today that proposal, as contained in the Senate staff draft, is for the creation of Regional Energy Services Commissions, an idea I never encountered before last week.

I have heard this proposal called innovative. I have heard it called radical. Regardless, it is certainly untested – in fact it has barely been discussed as to its potential impact on markets and competition. I find it hard to believe that this Committee is going to begin markup next week on a legislative proposal that has only been in the public domain for two weeks.

We oppose the concept of RESCs as outlined in the Committee draft. We do so because we believe that a primary component of achieving more competitive wholesale markets is uniform rules that make it easier for buyers and sellers of electricity to meet and do commerce. From the perspective of industrial users who have multiple electricity-consuming facilities across the country, we envision an eventual market that facilitates the purchasing of power for numerous facilities from one source. Such a market would provide lower cost power, reduce administrative costs, and make American manufacturing facilities more competitive.

We base this position on the fact that the interstate transmission grid is divided into three interconnections, one in the East, one in the West, and one comprised of most of Texas. Within each interconnection, power is synchronized and flows without regard to state or regional boundaries. We believe consumers would benefit if access to power within any one interconnection were made easier, not more difficult. We believe the creation of RESCs as described in the Senate draft would hinder, not facilitate, the flow of power.

Accordingly we support the concept of a standard market design, though we certainly do not endorse every provision of the proposal FERC put forth last year. We want to make markets more consumer friendly. Allowing each region's transmission infrastructure and tariff rate design to be governed by an RESC rather than by FERC would balkanize the market and, as we see it, benefit nobody – certainly not consumers.

The creation of RESCs would create yet another layer of bureaucracy. Consumers, even if they are the largest corporations in the country, have limited staff time and money to participate in proceedings such as envisioned by the creation of RESCs. Utilities, on the other hand, have endless human and financial resources because, unlike corporations in competitive markets, they can pass those costs on to captive customers.

I have tried, without success, to find the creator of this radical, new, and untested proposal. Although I have been unable to locate its progenitor, I can be reasonably certain that it is no one in the consumer community. We urge the Committee not to adopt this proposal, at least until it can be studied in greater detail.

Reliability Standards

All of the bills under discussion, with minimal degree of variation, contain what is commonly referred to as "consensus reliability" language. Though we recognize that many disparate stakeholders have endorsed this section in one form or another, we do not believe that it is a true consensus document and we do not believe that it will, in fact, enhance reliability.

By way of background, ELCON was part of the process that developed, and endorsed, the original "consensus reliability" language roughly seven years ago. That language was unfortunately the result of a Christmas tree effort, as every stakeholder representative (including us) tried to add language to advantage their own particular group. Since then, when we have looked at that end product and subsequent revisions, we see that they all have similar flaws.

We recognize that this is an issue in which few Members have an interest. All Members – and all industry stakeholders – support increased reliability. Certainly we do. But we do not believe that this language will serve that purpose.

First, not one of the "reliability" proposals actually increases reliability – rather each establishes a regulatory process which is designed to authorize one organization to set standards that are supposed to maintain reliability. Although promoters of this language purport to model it on the securities industry, that model fails under scrutiny. For example, violators of rules promulgated by the National Association of Securities Dealers can be denied the ability to trade. It is unclear how violations and violators would be sanctioned or punished in the electricity industry. Clearly, removal from market activities would be difficult if not impossible when dealing with owners of interstate transmission lines. And, since electricity functions in "real time," violations of reliability rules would cause real, possible irremediable, damage before any action could be taken in response.

Second, the language in the four proposals grants deference (or provides a rebuttable presumption) to regional groups founded on an interconnection-wide basis. This is in response to demands from western officials that "the West is different." This may be, and in fact reliability rules recognizing these regional differences can be developed without granting statutory deference in the standard-setting process to any regional group. If the facts support a regional standard, that regional standard should be adopted. But by granting deference to one group, this language opens the door for deference to be granted to other groups (perhaps to one organized on an RTO-wide basis; perhaps to consumers who actually pay the bills). Creating deference of any kind will encourage the development of a regional, rather than a national, standard, and generally make it more difficult for power to move from one region to another. In essence, what is supposed to be a "standard" is no longer a "standard."

And third, for those truly interested in making wholesale markets more competitive, reliability should not be considered in a vacuum. The issues of reliability and commercial impact are inextricably intertwined. One would be hard pressed to imagine a reliability issue that did not have commercial implications, and vice versa. Reliability standards should not be developed without an examination of their impact on commercial practices. To do so is to invite the development of "reliability standards" that are in fact new trade barriers or disguised mechanisms for discrimination. Ideally the preparation of reliability standards and so-called commercial practices would be done by the same organization. This would ensure

compatibility between the two and maximize the benefits of both reliability and markets to consumers. The current bifurcation of duties between the North American Electric Reliability Council (NERC) and the North American Energy Standards Board (NAESB) has a number of problems. For consumers and new entrants to the market, participation in NERC and NAESB standard-setting processes entails a considerable outlay of staff and other resources. Moreover, the fact that reliability and commercial practices will be made by two different organizations will lead to all sorts of complications and inefficiencies. We continue to believe that one organization, tasked with both standard-setting responsibilities, should consider both reliability and commercial practices.

In conclusion, we support a clear and short statement that FERC has the responsibility and authority to assure reliability and to consider the commercial impact as well. Everyone wants reliability. We believe it is worth the time to develop the legislative language that will truly achieve it. The legislative proposals before the Committee today will not accomplish what we are seeking.

Open Access (FERC-Lite)

FERC jurisdiction or the equivalent over currently non-jurisdictional utilities is an important issue if the transmission grid is to be operated in a truly open matter. We are pleased that over the past several years non-jurisdictional utilities have seen fit to agree to many concessions. Optimally, at some point, the entire grid, regardless of its ownership, will in fact be open and subject to uniform rules and regulations.

Transmission Siting

Generally speaking, ELCON supports giving FERC a right of eminent domain for siting of electricity transmission lines similar to that enjoyed for the siting of natural gas pipelines. That having been said, we certainly recognize the political problems with such a position and find the language in the House draft to be a reasonable approach. We understand that in fact states have not been the principal reason for delay in siting and building new transmission lines. But having a "fallback" right of eminent domain, as laid out in the House draft, while perhaps rarely used, would provide a motivation to ensure that state inaction does not occur.

Transmission Investment Incentives

The Senate staff draft, as well as the House draft and last year's October 16 draft, all address the need for new transmission. We believe that there is a need for new transmission in some regions, but not in all. The directive in these pieces of legislation that FERC implement and utilize incentive rates for the construction of all new transmission seems unnecessary and overly restrictive. If FERC believes that incentive rates are necessary – a decision that can and should be made on a case-by-case basis – they have sufficient authority to order such rates under present law. In House hearings, witnesses from both Goldman Sachs and for-profit transmission companies testified that such incentives are not needed in every case.

There certainly is no reason to provide incentives in areas where new transmission is not needed. Such efforts would merely reward monopoly transmission owners and increase costs for consumers.

In areas where new transmission is needed and cost recovery is assured, it is intuitive that the risk involved is very low. Utilities enjoy an almost ironclad guarantee that they will receive both a return "of"

and a return "on" their transmission investments. If the risk is low, i.e., the new transmission will be fully utilized, presumably a just and reasonable rate of return, not an incented one, is appropriate.

A recent study undertaken at the request of the National Association of State Utility Consumer Advocates attempted to quantify what these incentive rates would mean to consumers. According to an affidavit filed at FERC, consumers would pay $711 million per year, or $13.5 billion over the next 19 years, if incentive rates were to be the norm just to build transmission that would be built anyway. Looked at another way, that would be $13.5 billion of ratepayer money that would not be invested in new transmission infrastructure. On behalf of all consumers, industrial, commercial and residential, I find that objectionable, especially since the North American Electric Reliability Council has stated that significant new transmission will be built regardless.

Transmission Cost Allocation (Participant Funding)

The House bill's language on participant funding is less restrictive than language in the Senate draft and the language circulated last year. But participant funding ought to be a regulatory issue, not a legislative one. FERC has – and frequently uses – the authority to order such funding on a case-by-case basis. There is no reason to lock into statute an inflexible plan that mandates how transmission costs are to be assigned now and forever.

As a practical matter, it is nearly impossible to determine who will benefit from transmission upgrades, and it is inevitable that such beneficiaries will change over time. In addition, since nearly all stakeholders agree that new transmission is necessary in some areas, I question why Congress would adopt a plan such as participant funding that will likely retard the growth of new transmission. All consumer groups and all non-utility generators – the groups most likely to suffer if new transmission is not built – believe that mandating participant funding will hinder, rather than help, the construction of new transmission. If there is an electricity title in legislation, we hope Congress will be silent on this issue.

Transmission Organizations/RTOs

Industrial users know from experience that the transmission grid is the lynchpin to the creation of truly competitive wholesale electricity markets. If monopoly utilities can continue to use the transmission grid to benefit their own generation and deny access to power generated by others, we will never see wholesale competition in any real way.

ELCON has supported FERC's efforts to make the grid more open for many years. We support large, independent Regional Transmission Organizations (RTOs) with the day-to-day responsibility of running the grid (under FERC oversight). In order for an RTO to operate effectively, it needs independent governance so that monopoly transmission owners cannot develop self-serving rules and regulations.

We are, in fact, a little disappointed that FERC now seems more positively disposed to smaller RTOs than those originally envisioned. The greater the number of RTOs, the more important the "seams" issues become. "Seams" is just another word for barriers. How power goes from one RTO to another – through the seams, so to speak – is an issue that can greatly effect whether consumers have access to low-cost power or not. The proposal to create RESCs could make that "seams" issue into a "walls" issue.

Ideally an RTO would have administrative responsibility over all transmission, regardless of whether it is publicly or privately owned. It would also be responsible for the economic dispatch of merchant utility-

owned generation within the RTO footprint. We believe the language in the House draft provides a positive first step toward ensuring that federally owned transmission does not become the hole in the doughnut.

Although its efforts have not been perfect, we hope that Congress does not restrict FERC in its efforts to make the grid open and non-discriminatory. Legislation is not needed on this issue, other than perhaps to reaffirm FERC's authority to act.

PUHCA

Let me begin my comments on PUHCA by stating that I understand all too well why investor owned utilities have spent literally millions of dollars in lobbying and communication efforts over the last ten or so years to repeal PUHCA. It should be equally understandable why no *bona fide* consumer group supports PUHCA repeal. PUHCA is the primary federal statute available to address the abuse of market power by utilities that operate in more than one state.

Proponents of PUHCA repeal argue that the statute is outdated – an anachronistic law that no longer applies to today's utility markets. I argue that it is needed at least as much today as it was when it was enacted, in conjunction with the Federal Power Act, in 1935. In fact, in some ways PUHCA should be strengthened.

Indeed the current market structure, with so many regulated utilities having unregulated subsidiaries, provides a situation ripe for abuse. In fact no less a pro-business newspaper than the *Wall Street Journal* ran an article last December describing how utilities were taking debt from their unregulated enterprises and shifting it to their regulated entities so that ratepayers, rather than shareholders, were assessed the costs. PUHCA's language on cross-subsidization ought to be strengthened, rather than repealed, to protect consumers.

Similarly, taped conversations between energy traders of a major company dramatically depict how consumers were gouged during the Western power crisis. Congress should not repeal PUHCA but rather enact needed legislation to make it unlawful for any entity, directly or indirectly, to undertake fraudulent, manipulative, or deceptive actions in wholesale energy markets. Such language was included in HR 5614 last Congress; it is not included in any of the four bills before this Committee today.

A discussion of PUHCA is not complete without a discussion of mergers. Retaining FERC's merger review authority is essential given the number of recent utility mergers and the consolidation of the industry into a few large regional (and multi-regional) players. States and the federal antitrust agencies cannot do this – FERC therefore must be the fallback for this essential consumer protection. FERC also adds special expertise to the examination of these mergers.

Finally I would add that maintaining PUHCA as a federal statute is necessary not just to protect consumers but to protect investors. At present roughly forty percent of all power companies are listed on Standard & Poor's CreditWatch as having a negative outlook. More than 13 percent of all energy firm's have non-investment grade securities. On behalf of all consumers, we ask that you not repeal PUHCA at this time.

PURPA

Although PUHCA and PURPA are very different statutes, they are similar in that each gets a bad rap because of constant utility criticisms. And each has been the subject of extensive lobbying by utilities to achieve its repeal.

Utilities claim that they are mandated, under PURPA, to purchase power from cogenerators and other renewable energy resources. They claim that such power is often available at a costly price. But they don't tell you that rates were approved by each state utility commission. They don't say that the cost of wholesale electricity has gone down since PURPA was affirmed by the Supreme Court in 1982. And they don't tell you that Qualifying Facilities which sell power under PURPA are far more energy efficient and environmentally beneficial than the conventional base load power plants owned by utilities.

The Administration has recognized the benefits of cogeneration and combined heat and power (CHP) and has established a national goal of doubling our CHP output by 2010. It is totally inconsistent to endorse this objective and then repeal the mandatory purchase and sale requirements of PURPA.

ELCON addresses this issue from two perspectives. First, many of our members cogenerate power on-site, sometimes for their own use, sometimes to sell, most often a combination of the two. They know that the mandatory purchase requirement of PURPA is necessary until there are truly open wholesale markets for cogenerators to sell into. Otherwise utilities – who routinely obstruct the development of customer-owned generation – will not buy cogenerated power or will use their market power to keep such electricity off the grid. Until that time, PURPA guarantees are not just desirable, they are essential.

Similarly, the PURPA requirement that monopoly utilities supply back-up power to cogenerators at just and reasonable prices is necessary until there is a competitive retail market in which to purchase that power. Without a guarantee of back-up power, cogenerators cannot operate and the manufacturing facilities connected to it become useless.

Second, all of our members are consumers – and big consumers at that. It is noteworthy that those companies that pay the largest electric bills in the nation recognize that PURPA was the first federal statute to inject any competition into the electricity marketplace. PURPA is at least partially responsible for the decrease in electricity rates over the years. Industrial consumers believe it would be both shortsighted and harmful to repeal in any way the guarantees available to cogenerators under Section 210 of PURPA.

The language that the full Senate approved last year, in the Carper-Collins amendment, demonstrated the support that cogeneration enjoys. Similarly, the House Subcommittee on Energy and Power approved by voice vote the language now in the House draft. Both Carper-Collins and the House language recognize that PURPA protections should stay in place until working, competitive markets are available. We hope this Committee adopts a similar approach should it approve legislation. Retaining present law would also be acceptable if the Committee chooses not to act on electricity issues.

Net Metering and Real-Time Pricing

As I stated earlier, many ELCON members are cogenerators utilizing a combined heat and power system, often fueled by a renewable resource. Our members strongly support the concept of net metering as long

as it does not require the disclosure of proprietary information or intrude upon the internal operations of a company's generation activities.

Real-time pricing is a much more complicated issue than generally considered. Utilization of real-time pricing is a necessary but not sufficient condition to ensure that there is a functioning demand market (in contrast to demand programs as is generally the case in demand side management). All end users, and especially large end users, can assist in times of peak demand and congestion by reducing consumption. In real terms, a kilowatt hour of reduced consumption has the same effect as a kilowatt hour of increased generation. Many large industrial users are willing to play such a role assuming that compensation is appropriate. Real time pricing would be helpful in determining those levels, but only sophisticated consumers can assume the high risk of such actions. Hence, it is extremely important that real-time pricing is voluntary and not mandated on any customer class.

Finally, it should be noted that requiring end use customers to purchase power under only real-time prices transfers all risk from the utility to the customer. If a utility requires real-time pricing, its risk is lowered and, we believe, its potential rate of return should be reduced as well.

ELCON does not recommend that legislation address the issue of real-time pricing.

Market Transparency, Anti-Manipulation, Enforcement

The language in the Senate draft on information availability, disclosure requirements and the prohibition of round-trip trading are all good as far they go. But they don't go to the heart of the problem which is each utility's ability to exercise market power, the ability of a utility to manipulate markets, and the lack of significant market enforcement by any federal agency. These issues are related to the PUHCA issues discussed above. If Congress is to address this issue, it should take large steps, not small ones, and the steps should make markets more competitive and remover barriers to entry by new participants.

Consumer Protections

The issues found in the Senate draft and other pieces of legislation regarding slamming and cramming affect residential consumers far more than industrial. They are valid concerns and should be addressed.

Other Issues

An issue that has been the subject of much recent dialogue, including discussion at the recent House Subcommittee markup, is "economic dispatch." The basic question is whether utilities should dispatch (put on the grid) the lowest cost power available, even if it is not from their own generating facilities. Many utilities refuse to do so, claiming that they are protecting their customers or "native load." However, this claim fails. As a witness representing some of the largest customers in America, I can assert that we would certainly prefer to see the lowest cost power be made available whenever possible. Although I can understand why utilities try to protect their own generation, this practice is not beneficial to consumers and also discriminates against non-utility generators.

Conclusion

As I stated at the outset, we support competitive electricity markets. However, many of the proposals put forth in the Senate draft and in other legislation would not only make the market less competitive, it

would stifle the buds of competition that we have seen emerging in recent years. We support positive legislation that encourages markets to develop and removes barriers to new entrants. But quite honestly, we do not see that emerging from this Congress. That is why we believe that no electricity language may well be the preferable option, and that no electricity language may in fact be the most positive way to promote competition.