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THE ELECTRICITY COMPETITION AND RELIABILITY ACT

HEARINGS

BEFORE THE

SUBCOMMITTEE ON ENERGY AND POWER

OF THE

COMMITTEE ON COMMERCE
HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

ON

H.R. 2944

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THE ELECTRICITY COMPETITION AND RELIABILITY ACT

TUESDAY, OCTOBER 5, 1999

HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON ENERGY AND POWER,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2123, Rayburn House Office Building, Hon. Joe Barton (chairman) presiding.

Members present: Representatives Barton, Bilirakis, Stearns, Largent, Burr, Whitfield, Rogan, Shimkus, Wilson, Pickering, Fossella, Bryant, Hall, McCarthy, Sawyer, Markey, Pallone, Gordon, Rush, Wynn, Strickland, and Dingell (ex officio).

Staff present: Joe Kelliher, majority counsel; Cathy Van Way, majority counsel; Miriam Erickson, majority counsel; Ramsen Batfarhad, economic advisor; Sue Sheridan, minority counsel; and Rick Kessler, minority professional staff.

Mr. BARTON. The Subcommittee on Energy and Power will please come to order.

Today, we are going to begin the first of 2 days of hearings on H.R. 2944, which is a comprehensive piece of legislation to restructure the utility industry and the generation and transmission of electricity in the United States.

The Chair wishes to inform all members that we are going to adhere to regular order. We will recognize the ranking members and the subcommittee chairman and the full committee chairman for a 5-minute opening statement today. All other members will be recognized for 3 minutes. If there are members not present, their statements will be put into the record in their entirety. Tomorrow, we don't plan to have opening statements other than a brief introduction of our witnesses.

The Chair would like to recognize the distinguished ranking member, Mr. Hall, for his opening statement.

Mr. HALL. Mr. Chairman, thank you, and members of the committee. We have reached a milestone in the subcommittee's consideration of restructuring legislation with this legislative hearing today. This is a hearing that we have needed and that we have looked forward to.

I want to congratulate Chairman Barton. His efforts have really been tireless. He has made trips to all parts of this country to hear people and to keep an open door and to bring this subcommittee to the point we have reached here today, this morning.

And you have shown and extraordinary amount of leadership, Mr. Chairman, working with all of us and attempting to move this legislation through, to give the committee the right to work its will, and regardless of what the final outcome is of this legislation, your efforts, Chairman Barton, have advanced the public debate and our understanding of these very difficult and complex issues. I think you have done us a real service already.

I plan to listen carefully to the witnesses over the next 2 days to see whether we can find a common ground on which to move forward. I have particular concerns over what authority FERC should have in determining shape of the bulk power market of the future—is my time up already? Your beeper works—and I am pleased that you have asked the entire Commission to appear before us today.

I believe their expertise and insights will be particularly valuable at this point in our consideration of the legislation. They, like us, are of different minds about many of the issues before us, but unlike us, they have spent many, probably more, waking hours examining and deliberating these issues, and I am sure their testimony will be informative and instructive to us.

Other witnesses represent States and State officials. State preemption is a huge issue in this legislation. As a former county judge and former State senator, I have a strong bias against preemption of State authority. Preemptive provisions in this legislation will have to be accompanied by compelling reasons for exercising Federal preemptive authority, and that is what we will probably hear today.

By singling out these issues, I by no means intend to signal that other issues are not as important and deserve less attention. Our time and that of the witnesses is limited here today. It is more important that we hear from the witnesses.

With that, Mr. Chairman, I yield back my time and thank you.

Mr. BARTON. We thank the distinguished member from Texas and recognize Mr. Stearns for a 3-minute opening statement.

Mr. STEARNS. Five minutes?

Mr. BARTON. Three.

Mr. STEARNS. Mr. Chairman, thank you. I think when we look at this restructuring of some of the major issues, I think there is a consensus for prospectively repealing the Public Utility Regulatory Policy Act and provide for recovery of mandated costs, repeal the Public Utility Holding Company Act, apply FERC authority over non-jurisdictional entities, ensure transmission reliability, retain State authority to order competition, and encourage competition through State reciprocity.

You know, I think this bill that we have looks at most of these core issues and addresses them. Now, not everybody is going to be happy with this bill. When we come to restructure an over $200 billion industry, you are not going to strike a perfect masterpiece on the first brushstroke.

I wanted to point out, Mr. Chairman, Michigan has an interesting program called Electric Choice. It is a multiphase program allowing the States to adopt lessons learned in competition. The first bid phase alone brought in 117 requests from customers, power marketers, and associations to participate as competitive

electric providers. In Illinois, 430 of Comed's business customers have signed up to receive power from other registered suppliers. So, competition also affects States that haven't deregulated.

And the States are doing an excellent job. If we are to enact Federal legislation on this issue, we have to respect their hard work and success. As I said earlier, we don't have a perfect bill on the first attempt, but I am sure through the hearings like today, we will.

Our purpose today is to hear everybody, get their input, and to go and try to fine tune our efforts and understand what it takes to get a more perfect regulatory bill.

Judging from the people in the audience and the people standing out in the line, I can say that this must affect a lot of people, Mr. Chairman, so I hope that we move deliberately, and, most importantly, we respect some of the States who have already started reform in our approach to this bill.

And I yield back.

Mr. BARTON. We thank the gentleman from Florida.

I would like to recognize the gentleman from Ohio, Mr. Sawyer, for a 3-minute opening statement.

Mr. SAWYER. Thank you very much, Mr. Chairman. Thank you for your conduct of these proceedings throughout this year. It has been a long and I think constructive year, and thank you also for the introduction of a comprehensive bill to serve as a baseline for where we go to from here.

We really are at a critical juncture. I guess I would agree somewhat with the gentleman from Florida. I don't expect to find a perfect bill. I do hope that we can find a consensus bill, one that perhaps not everyone is happy with but which we can share some hope for that will work over time.

And that is really what is at stake here. Over the past century, electricity has powered virtually a second American revolution and has defined who we have become in this century. Through law and practice and policy, sound regulation has made this possible. It has evolved over time. And that century-old system, quite to the contrary of some of the rhetoric we heard at the beginning of the year, has served us well, I believe. It has brought us to the juncture that we are at today.

I think it is also fair to say that properly arrayed competition will bring better service at lower prices to the vast majority of Americans. Our job is to develop a regulatory framework in such a way that it accommodates changing technologies in a dynamic, competitive set of markets. The key to success, in my view, will be the adequacy of the transmission system. The grid is the backbone and the lifeline of competition.

The structure of the network really exists only as a product of evolutionary happenstance over the last century. It works. Various transmission components border upon one another, and electricity flows between them. But as a system, it was never designed as part of coherent regional transmission plans, which is what we need to build into the future.

The legislation that we are working on needs to anticipate that to handle the enormous flow of electricity across broad geographic areas and to anticipate the variability of the need for capacity and

at the same time to allow it to grow and be fully maintained and physically secure. A grid that lacks capacity or that limits growth, limits commerce.

To encourage the growth of those markets, I believe that Federal legislation should promote new investment so that the grid can grow responsibly, and the Federal framework must embody several basic principles. First, it should encourage the formation of RTOs, regional transmission organizations, but not mandate the structure of the transmission business. We have all said one size does not fit all, but a single template to meet the needs of diverse markets is going to be a difficult thing to undertake, and we may well all not hit it right the first time. We should anticipate the need for it to change.

We should encourage the expansion of transmission investment. We should expressly recognize the importance of expansion and the necessity and cost of maintaining and improving the reliability of electric service. It seems to me that——

Mr. BARTON. The gentleman's time is unfortunately expired. By unanimous consent, the gentleman from Ohio is recognized for another 1 minute.

Mr. SAWYER. I would be happy to——

Mr. BARTON. I like what you are saying, so I want you to keep going.

Mr. SAWYER. Okay. I am trying to go as fast as I can. I am saying a whole lot less than what I have got down on the paper here.

Mr. BARTON. I understand.

Mr. SAWYER. I appreciate the chairman's flexibility.

The Congress should set standards for establishing rates to cover transmission costs and to provide incentive to encourage the expansion of the grid.

It is also important, it seems to me, that transmission systems not be subject to shifting and contradictory regulatory jurisdictions and the requirements that come about as a result of that. It seems to me that FERC ought to have jurisdiction over all transmission. It may not be the same jurisdiction that it has today, but it should be broad jurisdiction, including unbundled transmission sold at retail. It should be expanded to cover all transmission service and interstate commerce; in short, to create a classic level playing field. Everybody ought to be involved in that regardless of the original genesis of their generating business.

I recognize the chairman has set some more goals. I am going to truncate what I have to say—the rest of what I have to say and insert it in the record. But just let me suggest that Federal legislation ought to ensure that transmission networks grow in step with competition. If they can't do that, if we can't build a prospective opportunity for this system to change, it seems to me that we will have missed the opportunity that the competition presents.

With that, Mr. Chairman, I thank you for your flexibility and yield back what small fraction of time I may have left.

Mr. BARTON. We thank the gentleman from Ohio.

We now recognize one of the most tireless members for restructuring, Mr. Largent of Oklahoma.

Mr. LARGENT. Thank you, Mr. Chairman. I want to commend you, your staff, the committee staff for the professional and open

manner in which H.R. 2944, the Electricity Competition and Reliability Act, has been assembled. To reach the point of holding today and tomorrow's much anticipated hearing on the bill before us, the subcommittee this year has held 11 hearings and received testimony from 92 witnesses examining the myriad of issues that constitute electricity restructuring.

Having worked on comprehensive electricity restructuring for over year, it is critical that Congress pass Federal legislation in the very near future to compliment the retail competition plans that 24 States have already enacted. My own State of Oklahoma, a State with relatively low electricity costs, has recognized the benefits that will flow from a competitive marketplace and has adopted its own restructuring legislation. The importance of Oklahoma's own retail competition plan, when coupled with Federal legislation promoting wholesale competition, should result in what is tantamount to a second land rush in terms of the beneficial economic impact it will have attracting new business to my State.

At a national level, competition will grant consumers the ability to reduce their electricity bills by choosing their electric provider. Savings are estimated to be the equivalent to a 5 percent income tax cut for a family of four. What about the examples of other monopoly industries? Following the deregulation of long distance telephone service, airlines, trucking, and railroad, the lowest price reduction was 28 percent.

Taxpayers will also save money. The National Taxpayers Union concluded that electric restructuring could save the Federal Government anywhere from $31.4 billion to as much as $75.6 billion over the next 5 years.

Witnesses before this subcommittee have stressed the fact that electrons do not distinguish between State or service territory boundaries. Electricity is an industry that is basically interstate commerce. We need to recognize this phenomenon and create a Federal regulatory structure that will provide a much more consistent national power grid. By doing so, we can design a national reliability standard to prevent regional reliability lapses such as those that occur during the blackouts in the Midwest this past summer.

I commend my colleagues on the subcommittee for their thoughtful insight and constructive input on this legislation. I will remind you that there have always been skeptics when Congress tackled complicated deregulatory efforts in the past, but Congress has been successful to the surprise of the naysayers. Now is the time to move forward.

I yield back my time, Mr. Chairman.

Mr. BARTON. We thank the gentleman from Oklahoma.

The gentleman from Massachusetts who has also been tireless in his efforts to open up the electricity grid, along with Congressman Largent, Mr. Markey is recognized for 3 minutes.

Mr. MARKEY. Thank you, Mr. Chairman. Powerless probably more than tireless.

I have watched with growing discomfort over the last 4 months as what began as an attempt to break down the regulatory barriers that have protected electric utility monopolies from competition has been transformed into legislation which would effectively defend

and extend the power of the existing monopolies and stifle the emergence of competition. This is an astounding and deeply troubling transformation. It is as if the majority, having lost sight of the original objective, now has resolved simply to redouble its efforts to get a bill.

What kind of a bill? The product that has emerged from the majority's internal discussions might best be called the electric futility legislation for it likely will render futile the best efforts of competitors to enter into the monopolist's closed markets and prevent consumers from getting lower prices through real price competition.

It pains me to reach this conclusion for I strongly support Federal legislation to promote competition in the electric utility industry. In fact, there may be no one on this side of the aisle who more strongly supports the objective of enacting Federal restructuring legislation, and I have always felt that it is not a partisan issue. I have tried to work closely with the gentleman from Oklahoma, Mr. Largent, the majority whip, Mr. DeLay, so that we can do it on a bipartisan basis.

Unfortunately, something seems to have gone very wrong with the product before us. This is really not a competition bill any longer; it is a monopoly bill. It does not demonopolize the utility industry; it deregulates the monopolies in a manner which will free them to engage in a wide array of unfair, predatory, and manipulative practices; practices which would stifle the emergence of competition and leave consumers paying more than they should for their electricity.

Let us look at some of the specific problems with this bill. It fails to give FERC authority to monitor, investigate, and correct anticompetitive behavior in generation markets. It repeals PUHCA 12 months after enactment, before the provisions intended to promote competition are in place, before many States can enact any new authorities that might be required, and without giving FERC and the States the full books and records authorities they will need to protect ratepayers against cross subsidies. It fails to address the ability of utilities to leverage revenues and resources from their monopoly functions to subsidize competitive ventures which allow the monopolies to unfairly compete against independent businesses.

It would allow for the creation of a two-tiered system of transmission use in which utilities could grant themselves preference for their own use and competitors would be unable to fairly, effectively, and efficiently utilize the transmission grid. It would allow utilities to reclassify transmission facilities as distribution and thereby evade FERC jurisdiction even when such facilities are truly part of the interstate network.

Mr. BARTON. I hate to interrupt the gentleman. I am not quite as thrilled to hear what he is saying—but he has the right to say it. But if he could sum it up in about 1 more minute, we would appreciate it.

Mr. MARKEY. It is a long list——

Mr. BARTON. I understand.

Mr. MARKEY. [continuing] but I will get—I can go to the highlights.

It would allow a closed club of utility monopolists to control and dominate regional transmission organizations and would not give

RTOs the powers needed to assure open and efficient operation of the transmission system. It directs the utilities to provide competitors with interconnection and then fails to expressly preclude utilities from favoring their own generation plans over those of competitors in future connection requests. It inserts a poison pill into the consensus reliability language by allowing States to develop reliability standards that may conflict with the national standards. There is no effective environmentally sustainable renewable energy generation technology or energy efficiency language in the bill.

In whole, this bill heads in just the opposite direction on just about every point. I do not believe that this stance musters as an anti-monopoly bill which ultimately is what competitors and consumers will need if they are to get the full benefits of a national electricity marketplace.

I thank you, Mr. Chairman.

Mr. BARTON. We will put the gentleman from Massachusetts as an undecided on the bill, correct?

The gentleman from Illinois, Mr. Shimkus, is recognized for 3 minutes.

Mr. SHIMKUS. Thank you, Mr. Chairman. Now that we have had our dose of sunshine for this morning, I want to thank you for working together on this draft legislation. I do say draft legislation and just want to remind folks here in the audience and people to testify that we sat probably for 2 months in a working group, which was bipartisan by invitation. Maybe two members of the democratic aisle came and attended those religiously—Congressman Hall, Congressman Sawyer.

Then I know the chairman very openly, when we dropped the first draft and also the second draft, asked for a bipartisan meeting to talk over the individual aspects of the draft legislation but was told no by my colleagues and friends on the other side, which is frustrating for me to hear all the problems with the draft legislation but not the willingness to come and sit down at a table to address these issues.

So, I want to commend my colleague and chairman for doing the best he can to work through a lot of these issues. We have moved great distances from a date certain aspect of the last Congress to a point where that is not even going to be an aspect mentioned as far as part of the legislation. I think that is positive. In the State of Illinois, we have moved great distances based upon an Illinois deregulation bill.

I plan on asking numerous questions today and tomorrow outlining some concerns with the legislation, but I do want to thank the chairman for the reciprocity language that has been changed based upon the second draft, especially for the State of Illinois.

There are some issues that, again, I will address as far as there are some Illinois that still think the grandfather clause needs to be strengthened to avoid accidental Federal preemption. I am hearing from Commerce Commission that some provisions still preempt State authority such as section 702 on net metering and section 101(e) on sections designed to give FERC authority to determine the function of power lines.

I am also hearing about fair competition between propane dealers and electric coops. Are coops cross subsidizing their propane

business particularly in States where they are self-regulated or is that just a perceived threat? I hope we get some answers in these 2 days of hearings. I think this should be examined.

There are additional issues which I plan on bringing up, but in the interest of time and efficiency, I will yield back my time and listen closely to the testimony today.

Thank you, Chairman Barton.

Mr. BARTON. Thank the gentleman from Illinois.

And we recognize another distinguished gentleman from Illinois, Mr. Rush, for a 3-minute opening statement.

Mr. RUSH. Thank you, Mr. Chairman.

Mr. Chairman, let me begin by commending you for the work that you have done to bring this important and significant legislation to the attention of the subcommittee.

I think all of us will agree it has not been easy, in terms of the number of consumers that will be affected. It could be easily argued that electricity restructuring is the most important work that the Commerce Committee has taken on since the deregulation of the telecommunications market. Those that were involved in that debate may recall that it was not until much work had been completed that legislation was finally passed out of the subcommittee and then the full committee, and eventually it was passed on the floor.

Mr. Chairman, I know the work that you have done. We have worked together on a number of issues regarding this legislation. Let me just say that the legislation before us accomplishes many things. It clarifies State and Federal jurisdiction under the Federal Power Act. It codifies FERC Order 888, and it provides for the formation of the regional transmission organizations, just to name a few things.

That said, Mr. Chairman, I must admit that I am not convinced that H.R. 2944 really accomplishes competition and reliability. For now, I will reserve judgment. I will listen intently to the testimony of the witnesses, and I will attempt to ask the appropriate questions. I will do this, Mr. Chairman, not to expose what the bill does not do but really to ensure that what we do do from this committee really and truly benefits our consumers.

Having said that, I am ready to move forward with the work of electricity restructuring but only if we do as the title of the bill suggests: Provide electricity reliability and electricity competition in addition to enhancing consumer service and consumer protection.

Thank you, Mr. Chairman. I yield back the balance of my time.

Mr. BARTON. Thank you, Congressman.

We now recognize the distinguished gentleman from North Carolina, Mr. Burr, for a 3-minute opening statement.

Mr. BURR. Thank you, Mr. Chairman. I thank you for this hearing, but, most importantly, and not to slight our other panelists, I thank you for the opportunity to have five FERC commissioners here to testify.

Mr. Chairman, it was Thomas Jefferson that said, "I am not an advocate of frequent changes in laws and constitutions, but laws and institutions must advance to keep pace with the progress of the human mind." We have an obligation to our Founding Fathers.

That was a warning to us all that as the human mind progresses, we have a responsibility as legislators to make sure that the system changes, the Federal system. We did that with the Telecommunications Act earlier this decade, and I think that to not accomplish this task would be a failure to what our Founding Fathers reminded us of.

I am extremely complimentary of you, Mr. Chairman, for perseverance as we have gone through this process. It has been a long road with many hurdles, and I think that we have reached a point where I am glad to say that we can move forward, and I am optimistic about the outcome. I think that this truly reflects the hard work of staff, of members, and of industry.

It is also refreshing to see that you have reached across the aisle as it relates to the participation by Mr. Brown, Mr. Wynn, and specifically, Mr. Sawyer, and others. I have personally co-sponsored Mr. Sawyer's transmission language, because I believe that it is the right language to have in place. I also realize that what we have today is not a final product, but it is a framework, a framework that all members can work within to find the right vehicle that can be created out of that.

Today and tomorrow we will solicit the advice, the instructions of our witnesses to try to refine it, to make sure that we have the right tools in place, and to discard those things that aren't needed. We will remove Federal barriers yet to competition, and we will create new incentives for competition.

Mr. Chairman, I am optimistic at the opportunity. I realize that there are varying views of what competition is. Some believe that competition can only be created when a Federal agency has the ability to regulate every step of competition. I am on the other end of that spectrum. I believe that without the free flow of electricity, not only from companies to consumers but without the regulatory burden of a Federal agency, will you in fact have true competition.

So, I encourage my colleagues to work to refine this language. I commend the chairman and the ranking member for this hearing, and I yield back the balance of my time.

Mr. BARTON. Thank the gentleman from North Carolina.

I would now like to recognize the distinguished ranking member of the full committee, the gentleman from Michigan, for a 5-minute opening statement.

Mr. DINGELL. Mr. Chairman, you are most courteous. I will try and comply with your wishes.

First of all, Mr. Chairman, I commend you for holding legislative hearings on this bill, H.R. 2944 of which you are the sponsor. It is a lengthy and comprehensive proposal dealing with issues of utmost importance to this very essential industry and its customers, and it warrants our very close attention.

Today and tomorrow, members are going to be hearing some severely conflicting testimony on the merits of what has been included in the bill, what has been omitted, and how its various provisions fit together. This last issue is not unimportant since the bill appears to draw on a number of prior proposals, and legislation of this significance must be internally consistent.

Mr. Chairman, as you know, I have been concerned that members of this committee have a sufficient grasp of the complex sub-

ject before us as they sift through the different arguments to determine what, if any, restructuring legislation should be enacted on the Federal level by the Congress. There has not been much agreement amongst the different elements of the industry, consumer groups, State and Federal regulators, and other interested parties.

I want to commend you for your effort to build the consensus necessary for legislation of this magnitude. The road to enactment is long, and it is important for members to find common and durable ground before reporting the bill. The issue is difficult, it is complex, and it is controversial.

If a consensus does not emerge from these hearings and if members on both sides of the aisle are comfortable going forward to a markup, then we will address those questions as they should be. However, if this is not the case, there will be little merit in forcing a markup simply to meet an arbitrary deadline. To do that guarantees us a fine fight and little opportunity of accomplishment.

It is not unusual, I would note, for major legislation to require many Congresses to mature. Notwithstanding the wishes of some of our honored guests, the time for enactment of legislation that will serve the broad public interest may not yet have arrived.

I want to thank you for the courtesy for your staff has extended to the minority in developing the witness list, and I look forward to hearing from the witnesses. It is important that we should have a complex piece of legislation heard with sufficient witnesses to gather broad cross section of the views as a people. I regret consideration of other legislation on the floor this week is not going to give me the time to spend at these hearings as I would like.

I would like to note that many questions remain to be addressed: reliability, whether or not conservation or environmental provisions should be included, consumer concerns, stranded costs, State responsibilities, State actions taken, State actions pending, job security, antitrust questions, needs to address the concerns of different components of the industry, including public's, TVA, Bonneville, and many others, and to do so in a way that takes care of the concerns and the needs of all.

This is not a simple industry; it is one which is composed of many different kinds of components, serving different customers in different ways in different parts of the country under different regulatory systems. And I would hope that as we go forward, we will consider that the impacts of this matter may not be simple.

I do thank you for your courtesy to me, Mr. Chairman, and I commend you for that way in which you are proceeding. Thank you.

Mr. BARTON. I thank the gentleman for that opening statement.

We would now like to recognize the gentlelady from New Mexico, Congresswoman Wilson, for a 3-minute opening statement.

Ms. WILSON. Thank you, Mr. Chairman, and I won't take 3 minutes.

I wanted to commend you for having this hearing and also for producing a bill in a way that was very open to input from all of the members of this committee and even those outside of this committee, and I appreciate that.

I think all of us recognize that this is an extremely complicated issue. There are a number of different facets to it, and the intent

of all of the members of this committee and also the Chair is to get this right, to make sure that a bill that eventually merges from this Congress enhances competition while protecting consumers and ensuring there is universal access to electricity for all Americans, including Americans in rural areas.

I just wanted to thank the chairman for holding this hearing and moving this bill forward, and I know there are many more things we have yet to work out, but I appreciate his leadership.

Thank you.

Mr. BARTON. I thank the gentlelady from New Mexico. The Chair would recognize the gentleman from Kentucky, Mr. Whitfield, for a 3-minute opening statement.

Mr. WHITFIELD. Mr. Chairman, thank you very much. I understand we have already had 11 hearings and 92 witnesses, and I want to commend the chairman for being very open in this process.

I am delighted this morning that I have a young woman from my hometown of Hopkinsville who is serving as one of the commissioners who will be testifying this morning, and I know that, along with her, both of us will be looking at this legislation and its impact on Kentucky which has some of the lowest electricity rates in the Nation. Also, 95 percent of our electricity is generated by coal fire processes, and any legislation on deregulation that passes obviously we are going to be very concerned about its impact on coal and on our rates.

And, so I look forward to the testimony this morning, and thank you for giving me the opportunity to be here.

Mr. BARTON. I thank the gentleman from Kentucky.

We are prepared to recognize the gentleman from New Jersey or we can go to Mr. Bryant and give you a few minutes to get settled.

We recognize the gentleman from Tennessee, Mr. Bryant, for a 3-minute opening statement.

Mr. BRYANT. I want to thank you, Chairman Barton, for this opportunity today to address this issue. I really do appreciate all the work that you have put into making this an open, deliberative process, and also I want to specifically thank you for honoring your commitment to do those things. You have been very kind to all of us, always ready to listen to what we have to say, and I especially appreciate your concern with those of us from the Tennessee Valley.

I do believe that the free market and increased competition can lead to better service and lower prices for consumers. However, I want to ensure that the thousands of residents and businesses in the rural areas across the country, not just in the Tennessee Valley, but across the country are not forgotten in this move to restructure. Our agricultural communities and small towns rely on reasonable electricity rates to keep their farming, their industries, and their small businesses alive.

As we work on this legislation, we must safeguard that balance between State and Federal Governments and must not create an immense Federal bureaucracy, such as FERC, in the name of deregulation. We must preserve both private and public power and promote diversity in generating sources from coal, natural gas, and nuclear to renewables such as hydroelectric and solar energy.

Although this legislation is concentrated on the national electricity picture, we must also recognize the differences as well as the similarities between regions of our country. I believe that we should give primacy to regional solutions. The one-size-fits-all Federal legislation would not recognize our different needs.

My home State of Tennessee is unique, because it is the only State in the country where wholesale competition cannot occur without Federal action, even though the Tennessee Valley Association has been very successful over the years in the region with helping out on navigation and the environment and flood control. I do not view myself as the primary defender of the TVA; rather, I believe that it is my role to be the defender of the citizens of Tennessee. I believe that we can craft legislation which will maintain inexpensive and reliable power for the people of our region.

Again, I want to thank Chairman Barton for his leadership on this particular legislation, and I look forward to continuing to work with the members of this subcommittee and the full committee to craft the right solution for restructuring, and I would yield back my time.

Mr. BARTON. I thank the gentleman from Tennessee for those words, and also thank him for the work that he has put into the TVA section of the bill. He has done yeoman's work in that area.

I now recognize the gentleman from New Jersey, Mr. Pallone, for a 3-minute opening statement.

Mr. PALLONE. Thank you, Mr. Chairman. I have many concerns regarding this bill, but I heard your 3-minute warning there, so I am cutting back some of what I was going to say.

I did want to say, though, that including my own State there are 24 States that have already restructured their electric utility sector, and I think we have to be extremely careful not to damage these States efforts or cause them to redo their legislation. Any grandfathering language must be crafted with the utmost care, and I hope our witnesses will address the implications of the provisions in the chairman's mark on States that have already passed restructuring legislation.

On State Federal jurisdiction, H.R. 2944 appears to essentially codify the 8th Circuit Court of Appeals decision which held that FERC cannot bar utilities from giving first priority in transmission service to their native load before providing capacity to other parties. This could jeopardize firm transmission service. The decision also could jeopardize mergers that depend on a reservation of firm transmission service.

In terms of reliability, the legislation has incorporated so-called consensus language. Some utilities believe, however, that this language is based on out-of-date models and goals and would undermine market efficiency and optimization. Any legislation we write should foster true competition and provide non-discriminatory access to the Nation's electric grid.

Overall, this bill does not appear, in my opinion, to be a true competition bill, and it seems that many entities and groups I have heard from agree that RTOs, regional transmission organizations, or ISOs, independent system operators, should encompass larger geographic regions to reduce the potential for market power abuses and to foster true competition. If market power is being exercised,

we must examine the process and rules under which the system is operating. Over 100 organizations have written and/or called me to express their concerns in this regard.

The other issue that is most important to me critical is environmental protection, and this bill is clearly lacking in environmental protection provisions. We cannot let this sector restructure at the cost of polluting our environment and endangering people's health. Fourteen Republicans have sent a letter to Chairman Barton emphasizing support for and demanding inclusion of environmental protections, and I will elaborate more upon this tomorrow when we have experts testify on this topic.

But on a related note, though, over 100 groups have written supporting the inclusion of a renewable portfolio standard and the public benefits trust, but these are not in the chairman's mark. These provisions go hand-in-hand to ensure universal service and promote the use of clean energy sources. Charges for public benefits have long been in consumers' utilities bill, and they would not be newly imposed.

So, I have highlighted, Mr. Chairman, some of the initial major issues that concern me with regard to this version of the chairman's mark, but clearly we all need time to examine the legislation more thoroughly, in my opinion, at both the macro and micro levels. I am interested in hearing out witnesses' analysis of the bill.

Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Congressman Pallone, and we—the Chair shares several of the concerns that you have addressed, and we hope this legislative hearing and the time right after it we can work together on some of these issues.

Seeing no other members present who have not yet been given an opportunity to give an opening statement, the Chair would recognize himself for his 5 minute opening statement.

The bill before the subcommittee is a very different bill than the bills that we have considered earlier in this session. This bill has no Federal mandate. This bill does not preempt States in areas historically reserved to be regulated by the States. This bill does focus on the core Federal issues that States have little or no ability to address.

We held our first hearing on this issue more than 4 years ago. Since then we have held 32 hearings, received testimony from 331 witnesses. This year we have held 11 hearings and heard testimony from 92 witnesses. There was one thing that every witness we have heard from this year has agreed upon, and that is that the need for the Congress to act in this session on electricity legislation.

There was another clear message from the hearings that we have held this year: The States have little or no ability to address certain core Federal issues, such as interstate commerce, foreign commerce, reliability of the interstate transmission grid, open access to the interstate transmission grid, the role of the Federal utilities in competitive electric markets, Federal and State jurisdiction, and reform of Federal electric and tax laws. Only the U.S. Congress can address these core Federal issues.

Some would say that we have deliberated too long. Mr. Markey says that he does not want any more seminars on electricity, and I agree. He just wants a final exam, and I agree with that also.

If I were at Indianapolis, I would say, "Ladies and gentleman, start your markup pens. The time has come to act."

The situation is clear: Change is sweeping across the electricity industry. States are opening their retail electric markets. Some utilities are voluntarily divesting themselves of generation; others are merging. New entrants are buying utilities. Federal electric laws that were written in most cases more than 60 years ago are simply not adequate for today's situation. Those Federal laws were based on the premise that States would always regulate retail electricity rates. That premise is no longer valid.

There is a cost to inaction. If Congress does nothing, problems that exist under the status quo will remain. Reliability will be at risk. The transmission system will remain subject to four different sets of rules. Transmission owners will retain the ability to discriminate against their competitors, and incentives to invest in transmission will remain inadequate. Consumers will be exposed to slamming and cramming by electric marketeers. The privacy of consumer information may not be assured, and consumers will not be assured access to the information that they need to choose among competing retail electric suppliers. The Public Utility Holding Act of 1935 will continue to discourage new entrants into the electricity industry. The mandatory purchase obligations of PURPA will remain in force and may require utilities to sign contracts to purchase power at above market rates. Disincentives in the Federal tax law will discourage State and municipal utilities and rural electric cooperatives from opening their transmission systems and retail markets. Payment of the Bonneville Power Administration's unrecovered power costs will remain taxpayer liabilities. The Tennessee Valley will continue to be the only region in the country where wholesale competition is prohibited, and distributors in the region will continue to be forced to buy their power solely from the Tennessee Valley Authority.

Ladies and gentleman, any one of these reasons is sufficient for the Congress to pass electricity legislation in this session of Congress. So, once again, I say, "Ladies and gentleman, please start your markup pens."

[Additional statements submitted for the record follow:]

PREPARED STATEMENT OF HON. MICHAEL BILIRAKIS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Thank you, Mr. Chairman.

First, I would like to thank you for scheduling two legislative hearings on your bill, H.R. 2944, the Electricity Competition and Reliability Act. There is little doubt that electricity restructuring is extremely complex. In 1999 alone, our Subcommittee has held eleven hearings and received testimony from 92 witnesses on the broad range of issues surrounding electricity restructuring.

Mr. Chairman, you should be commended for your attempt to draft a consensus restructuring bill. This was a truly herculean undertaking, and I appreciate your efforts to solicit the views of the Energy and Power Subcommittee members before introducing H.R. 2944.

As we continue to consider the restructuring of our electricity industry, it is important for us to have a thorough understanding of the impact any restructuring legislation could have on our current system. In this regard, I am anxious to hear the testimony of our witnesses.

They have a wide range of expertise, and I am sure their comments will provide us with some additional guidance on the complex issue of electric utility restructuring. Their analysis of H.R. 2944 should be very useful in our Subcommittee's discussions.

Mr. Chairman, I look forward to our continuing dialogue on H.R. 2944 and electricity restructuring.

Thank you, Mr. Chairman.

PREPARED STATEMENT OF HON. TOM BLILEY, CHAIRMAN, COMMITTEE ON COMMERCE

Mr. Chairman, I am happy to be at today's legislative hearing on H.R. 2944. As you know, I have been a supporter of comprehensive electric utility restructuring since the early days of the 104th Congress and supporter of competition in the electric utility industry prior to the enactment of the Energy Policy Act of 1992.

Throughout this debate I have been concerned about one thing, that all consumers benefit. I have said many times both publicly and privately that consumers, not utilities, should be front and center in any restructuring debate.

As I look at the proposal before us, and listen to the testimony of the witnesses I will be concerned about one thing: "How does it impact consumers?" I want restructuring legislation to work for the suppliers, new entrants and incumbent utilities, for the reliability of the national grid—and ultimately for consumers. I believe our nation's retail customers have been captive ratepayers for too long.

I am hopeful that the federal government will be able to choose its supplier someday soon. The government is a big customer. Taxpayers will surely benefit when the Federal government starts to lower its monthly bill. Federal savings from restructuring are calculated at billions of dollars, so if there are any budgeteers in the room, I hope you are paying attention.

Mr. Chairman, I am happy to see you taking this important step and look forward to working with you as this bill moves through the Committee process.

Thank you.

PREPARED STATEMENT OF HON. ALBERT R. WYNN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. Chairman, I want to thank you for holding these hearings on electricity deregulation. The deregulation of the electricity industry is a critical issue that will affect every American. Today most of us take for granted the fact that our homes are temperature controlled, our lights turn on and off at the flip of a switch, and our appliances, fax machines and computers operate at our command. We do not think about where our electricity comes from or how it gets to our homes and offices. Yet electricity is a fundamental part of our day—without which most of us could not easily function.

A critical issue that we must consider is the role of the federal government and the jurisdiction of the states. The federal government clearly has a role but we must make sure that this role is limited to addressing only the truly federal issues. We should ensure that the interstate transmission system is adequate and reliable and remove barriers to competition such as PURPA and PUCHA.

Electricity deregulation legislation should not expand FERC jurisdiction into areas current under state jurisdiction or give FERC new authority that would undermine a competitive electricity marketplace. New regulatory authority given to FERC should be very limited and clearly defined. We don't need to "reregulate" if the underlying goal is to promote free markets and competition.

Any federal bill should refrain from dictating to states the details associated with implementing retail competition. Metering, billing, affiliate rules, consumer protection, universal service and a host of other issues should be left for resolution at the state level by lawmakers and regulators who are familiar with the specific needs of their states.

In Maryland, for example, our legislature passed in April an electric restructuring law that is very comprehensive. It will become even more detailed as the Public Service Commission provides the rules for implementing the legislation. Neither Maryland, nor any of the other 23 states that have enacted restructuring laws should be forced to go back to the drawing board re-write the rules for electricity deregulation issues that clearly fall within their jurisdiction and have already been dealt with by their state legislatures.

Our task is to find just the right balance that will encourage competition, yet leave the states with the flexibility they need to formulate plans best suited to their citizens.

PREPARED STATEMENT OF HON. BILLY TAUZIN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF LOUISIANA

Mr. Chairman, the legislation before us today is a good first step toward achieving competitive retail electricity markets nationwide. However, it proposes the outright repeal of PURPA upon "date of enactment." Unfortunately, this has significant negative implications for the many PURPA facilities that are in my Congressional district.

Many companies in my district built PURPA plants because they needed the electricity and steam to operate their manufacturing plants. They built these QFs (Qualified Facilities) because they could produce alternative forms of electricity for less than the price charged by the local utility. Low cost energy is essential to their competitiveness in domestic and international markets.

While it is true that QF reliance on "PURPA contracts" has created an artificial electricity wholesale marketplace, PURPA does provide QFs with important protections that should be preserved—at least until our electricity markets are competitive.

These protections include guaranteed access to interconnection, standby/back up maintenance power at just and reasonable prices, mandatory power purchase requirements and PUHCA exemptions. If we choose to abruptly withdraw these safeguards before realizing a competitive electricity retail marketplace, then we will have seriously compromised QF ability to secure debt financing of their operations. Frankly then, PURPA protections are needed now and will continue to be necessary until there is a competitive electricity retail market that will allow QFs the flexibility and choice that usually accompany competition. .

Don't get me wrong Mr. Chairman, I am in favor of repealing PURPA. However, I am inclined to support language which phases out the effect of PURPA over time as proof of retail competition across the country becomes more evident. Such language, I believe, would be fairer to the QFs than a provision repealing PURPA on date of enactment. At the same time, it would also make clear that the wholesale market inefficiencies created by guaranteed contracts are on the way out.

I look forward to working with you to reach a satisfactory outcome.

Mr. BARTON. With that, I am going to welcome our first witness, but before that, I noticed that we have all five of our FERC commissioners, and you all look very uncomfortable all scrunched up out there in the front row. We will be very happy to let you use the majority lounge. You can hear our first witness and hear the questions and answers and make some phone calls. You are welcome to continue there in the audience, but if you wish to—and I am sure the minority would welcome you into their lounge too; this is not a partisan—if some of you want to go to the left and some to the right, that is okay. But you are welcome, because we will be with the gentleman from the Department of Energy for probably the next hour or so. Okay?

Mr. Glauthier, we want to recognize you as our first witness of our legislative hearings. As the distinguished member of the Department of Energy and the No. 2 person at the Department of Energy, the Deputy Secretary of Energy, you have had quite a bit to do with the formulation of the Department's comprehensive bill. And although we are somewhat saddened that we couldn't have Mr. Richardson, we are delighted that we have you. So, we are going to recognize you for such time as you may consume, and then we will have some questions for you.

Welcome to the committee.

STATEMENT OF HON. T.J. GLAUTHIER, DEPUTY SECRETARY OF ENERGY, U.S. DEPARTMENT OF ENERGY

Mr. GLAUTHIER. Thank you, Mr. Chairman, Mr. Hall——

Mr. BARTON. And you need to really put that microphone close to you, sir.

Mr. GLAUTHIER. Thank you, Mr. Chairman, Mr. Hall, Mr. Dingell, and other members of the subcommittee. Thank you for inviting me here today to present the administration's views on H.R. 2944, the Electricity Competition and Reliability Act.

At the same time the Federal Energy Regulatory Commission continues to promote competition in the wholesale markets, 24 States have now adopted electricity restructuring proposals that allow for competition at the retail level. Almost every other State has the matter under active consideration. The Clinton administration believes that this is a positive development. Competition, if structured properly, will be good for consumers, good for the economy and good for the environment. However, the full benefits promised by competition can only be realized within an appropriate Federal statutory framework. What we do at the Federal level and when we do it, will have a profound impact on the success of State and local retail competition programs.

Mr. Chairman, I want to commend you and the other members of this subcommittee for the effort you are putting forth. Many of the issues are complex and controversial. Nevertheless, it is vitally important to consumers, the economy, and the environment that these issues be resolved in an appropriate manner.

I also want to thank you for the courtesy which you and your staff have shown to myself, Secretary Richardson and other members of the Clinton administration. I believe that working together in a bipartisan fashion, the administration and members on both sides of the aisle can achieve a result that will benefit all Americans.

Let me begin with three points: First, it is critical that Congress pass comprehensive electricity restructuring legislation soon; second, restructuring legislation can succeed only if it is developed on a bipartisan basis, and, third, although the bill includes some encouraging provisions, the administration cannot support H.R. 2944 in its current form, but we are willing to work together to achieve legislation that we can all support.

As the States continue to move forward, the absence of action at the Federal level is creating significant uncertainty in the increasingly regionalized power and transmission markets. The fact is, if we don't act, the benefits from State restructuring programs will be limited.

At the very least, Congress needs to extend FERC jurisdiction to all major transmission owners; it needs to clarify FERC's authority with regard to the formation of regional transmission organizations; it needs to authorize the development and enforcement of mandatory reliability standards to enable FERC to prevent incumbent utilities from using market power to inhibit competition; to ensure that public benefits programs, including renewable energy, low-income assistance, and energy conservation are not lost as a result of the transition to competition, to eliminate statutory impediments to State competition programs, and to enable competition to thrive in the regions served by Federal utilities.

Electricity restructuring is not a partisan issue. Members on both sides of the aisle have offered thoughtful and meaningful proposals that merit consideration, including a bipartisan bill introduced earlier this year by Congressmen Largent and Markey. Mr.

Chairman, we encourage this subcommittee to continue your efforts to develop a bipartisan bill that will enable Congress to enact comprehensive restructuring legislation that can be supported by the administration.

We commend you for including a number of positive provisions in H.R. 2944, such as those intended to enhance reliability, protect consumers, and promote aggregation. Clearly, your legislation addresses many of the key issues that need to be included in a comprehensive electricity restructuring bill. However, we believe that H.R. 2994 should be modified to establish the necessary ground rules and adjustments required for the transition to competition.

Given the time constraints of this morning, I would like to focus my comments on four important issues: First, market power; second, FERC jurisdiction over transmission; third, regional transmission operators, and, fourth, public benefit programs. My written testimony contains a more detailed discussion of the administration's views on H.R. 2944.

First, on market power. The primary goal of Federal electricity restructuring legislation must be to aid the transition to competition in a manner that allows consumers to benefit through lower rates. However, significant rate savings cannot be achieved if effective competition fails to develop.

Open transmission access and the creation of independent regional transmission organizations should go a long way toward achieving competitive markets. However, access to transmission is, by itself, not enough. Utilities that own substantial amounts of generation in a region or strategically located facilities may be able to influence prices and inhibit the entry of new competitors through horizontal market power.

Mr. Chairman, we are disappointed that H.R. 2944 fails to provide FERC with sufficient authority to address market power. We recommend that the bill be modified to incorporate the market power provisions in the administration's bill.

The second area I would like to speak to is jurisdiction over transmission. FERC Orders No. 888 and 889 have had a tremendous positive impact in promoting wholesale competition by requiring jurisdictional utilities to provide competitors access to transmission facilities under rates and terms comparable to those provided to itself. The administration supports the provisions in H.R. 2944 which extend FERC's authority to the transmission facilities owned by previously non-jurisdictional utilities.

We are concerned, however, that H.R. 2944 can balkanize the regulation of transmission in light of a recent 8th Circuit Court of Appeals decision. FERC may be unable to prevent a utility providing transmission services that are bundled with the retail sale and distribution of power from discriminating against other electricity suppliers in favor of its own generation.

State regulators, which would have jurisdiction over bundled transmission services, may not have sufficient incentives to adequately police a utility's use of its transmission lines.

Mr. Chairman, we strongly urge you to reevaluate this provision. We are not suggesting that FERC should regulate the rates for bundled transactions, but FERC should have the ability to ensure that all competitors have equal access to transmission resources.

The third area I would like to speak to is regional transmission organizations. Properly sized, independent, regional transmission organizations can provide significant benefits, including the enhancement of reliability and the promotion of more efficient and competitive markets.

The administration is encouraged that H.R. 2944 would require all transmitting utilities to join RTOs and we generally support the standards for RTO formation laid out in the bill. We are concerned, however, that the legislation limits FERC's discretion in approving an RTO. It is important that FERC be able to require the formation of an RTO that would be optimal for a particular region.

The fourth area is public benefits. Mr. Chairman, we commend you for recognizing the need to address renewable energy in restructuring legislation. We support both the extension of the Renewable Energy Production Incentive program for municipal and cooperative utilities and wind and biomass tax credits for investor-owned utilities. However, more does need to be done, such as the inclusion of a renewable portfolio standard. The progress we have made in renewables could be partially lost during the transition to competition because these technologies have not yet achieved full cost competitiveness.

In addition, we continue to be concerned that retail competition could lead to reduced support for programs that provide important public benefits. A public benefits fund, which provides matching funds to the States for low-income assistance, energy efficiency programs, consumer education, and the development and demonstration of emerging, clean technologies, should alleviate these concerns.

In conclusion, Mr. Chairman, while the States are proceeding with their restructuring programs, all eyes are on Congress to learn what signals the wholesale and retail markets will receive. This committee's leadership has been essential and will continue to be. Although we cannot support H.R. 2944 in its current form, the administration's approach to comprehensive restructuring legislation has many elements in common with your proposed legislation. And I know that several members of this subcommittee, on both sides of the aisle, have put forth proposals that also merit serious consideration.

We are confident that a bipartisan bill can be reported out of the subcommittee soon. Secretary Richardson and I, as well as our staff, and other members of the administration stand ready to assist you and the other subcommittee members in this vital endeavor. Only by working together can we take the steps that are necessary to provide consumers with the full benefits of competition.

Thank you, Mr. Chairman.

[The prepared statement of Hon. T.J. Glauthier follows:]

PREPARED STATEMENT OF T.J. GLAUTHIER, DEPUTY SECRETARY, U.S. DEPARTMENT OF ENERGY

INTRODUCTION

Mr. Chairman, thank you for inviting me today to present the Administration's views on H.R. 2944, the Electricity Competition and Reliability Act. DOE, the Agency responsible for formulating and implementing the Clinton Administration's energy policies, is a strong proponent of comprehensive Federal electricity restructuring legislation. On April 15, Secretary Richardson transmitted to Congress the

Comprehensive Electricity Competition Act (CECA)[1]—the Administration's vision for the role the Federal government should play in the transition to competition.

At the same time FERC continues to promote competition in the wholesale markets, 24 states have now adopted electricity restructuring proposals that allow for competition at the retail level. Almost every other state has the matter under active consideration. The Clinton Administration believes that this is a positive development. Competition, if structured properly, will be good for consumers, good for the economy and good for the environment. Companies that had no incentive to offer lower prices, better service, or new products will now compete for customers. Consumers will save money on their electric bills. Lower electric rates will also make businesses more competitive by lowering their costs of production. By promoting energy conservation and the use of cleaner and more efficient technologies, greenhouse gas emissions will be reduced, as will emissions of conventional air pollutants. However, the full benefits promised by competition can be realized only within an appropriate Federal statutory framework. What we do at the Federal level, and when we do it, will have a profound impact on the success of state and local retail competition programs.

Mr. Chairman, I want to commend you and the other members of this Subcommittee for the effort you are putting forth in an attempt to enact comprehensive electricity restructuring legislation. Many of the issues are complex and controversial. Nevertheless, it is vitally important to consumers, the economy and the environment that these issues be resolved in an appropriate manner.

I also want to thank you for the courtesy which you and your staff have shown to me, Secretary Richardson and other members of the Clinton Administration. I believe that working together, in a bipartisan fashion, the Administration and members on both sides of the aisle can achieve a result that will benefit all Americans.

Let me begin with three points:

- It is critical that Congress pass comprehensive electricity restructuring legislation sooner, rather than later.
- Restructuring legislation can succeed only if it is developed on a bipartisan basis. And
- Although the bill includes some encouraging provisions, the Administration does not support H.R. 2944 in its current form. We would like to work with you to achieve a version of restructuring legislation that we could all support.

FEDERAL ACTION IS CRITICAL

While some state competition programs are already in effect, tens of millions of additional consumers will soon have the ability to choose their power in those states implementing retail competition programs over the next 2-3 years. As the states continue to move forward, the absence of action at the Federal level is creating significant uncertainty in the increasingly regionalized power and transmission markets. The fact is, if we don't act at the Federal level, the benefits from state restructuring programs will be limited.

- First, competition is not going to work if transmission lines operate under different sets of rules and requirements. It is essential that all wholesale and retail power marketers have non-discriminatory access to the wires that transport their product. While the Federal Energy Regulatory Commission (FERC) has jurisdiction over the transmission of electricity in interstate commerce, FERC's authority is somewhat limited. Congress needs to ensure that all major transmission facilities are, to the extent practicable, subject to comparable FERC open access requirements.
- Second, independent regional transmission organizations (RTOs) will help promote efficient, competitive and reliable markets. However, FERC's authority over, and ability to require, RTO formation remains uncertain. Congress must address these uncertainties.
- Third, as we move to a more competitive environment, the reliability of our bulk power systems can no longer be entrusted to voluntary standards. Significant support has developed for a proposal to have an electric reliability organization, overseen by FERC, establish mandatory reliability standards. Congress should authorize the development and enforcement of mandatory reliability standards.

[1] The Administration transmitted CECA to Congress in two separate parts. The first part, which was introduced by Congressman Bliley and Dingell (upon request) as H.R. 1828 on May 17, includes all of the non tax-related provisions in the Administration's proposal. Both parts were introduced in the Senate by Senators Murkowski and Bingaman (upon request)—S. 1047 and S. 1048—on May 13.

- Fourth, restructuring efforts won't succeed if competitive markets are not developed. While open transmission access and the formation of independent regional transmission organizations should go a long way towards changing the monopoly structure of the electric utility industry to competition, the fact is that some utilities may have horizontal market power as a result of their control over a substantial amount of generating capacity, enabling them to crowd-out potential competitors and keep the price of power artificially high. Congress must empower FERC to prevent incumbent utilities from using market power to inhibit competition.
- Fifth, existing programs that provide support for renewable energy and other important public benefits were designed for a system of regulated markets. Congress should act to ensure that these public benefits are not lost as a result of the transition to competition.
- Sixth, certain Federal statutory provisions may impede the efforts of the states and FERC to promote competition. Congress needs to eliminate these impediments and modernize those statutes which are inconsistent with the development of fully competitive markets.
- Seventh, the statutes governing the operation and regulation of Federal utilities—the Tennessee Valley Authority (TVA) and the Federal Power Marketing Administrations (PMAs)—must be revised to allow for effective competition in the regions they serve.

Mr. Chairman, the Federal government clearly has an important role to play in the transition to competition. While the states are moving forward rather briskly, Congress has yet to act. The Federal government needs to send the appropriate signals about what the rules of the road will be in this new world of competition. Instead, we are sending signals of confusion.

The electricity markets are crying out for the certainty that is necessary before essential investments are made. Generating capacity reserve margins have significantly tightened. The construction of new major transmission facilities has dramatically slowed. Aging distribution facilities are beginning to wear out.

Several regions of the country have experienced major problems in recent summers. As the heat and humidity rose, some utilities found it increasingly difficult to meet consumer demands. Spot prices for electricity rose dramatically. Elected officials and utility executives made urgent public appeals for conservation. Factories were forced to shut down their operations and send workers home. Some areas experienced rolling blackouts. Other areas lost power due to failures in overworked and outdated distribution facilities. While it is difficult to attribute all of these problems to the uncertainties surrounding the transition to competition, they clearly have played a significant role. In short, Mr. Chairman, we can't afford to wait until the 107th Congress to do what needs to be done now.

NEED FOR BIPARTISAN APPROACH

The electricity sector is our nation's most capital-intensive industry, holding assets with a book value of approximately $700 billion. In addition, electricity affects our everyday lives and businesses. It is not at all a stretch to point out that access to power can sometimes be a matter of life and death. This is a major industry that is in the process of a monumental transition.

Very few major congressional initiatives are accomplished in the absence of a bipartisan approach and with cooperation from both ends of Pennsylvania Avenue. Mr. Chairman, electricity restructuring is not a partisan issue. Members on both sides of the aisle have offered thoughtful and meaningful proposals that merit consideration, including a bipartisan bill introduced earlier this year by Congressmen Largent and Markey. DOE encourages you to continue your efforts to develop a bipartisan bill that will enable Congress to enact comprehensive restructuring legislation that can be supported by the Administration.

COMMENTS ON H.R. 2944

Mr. Chairman, we commend you for including a number of positive provisions in H.R. 2944, such as those intended to enhance reliability, protect consumers and promote aggregation. Clearly, your legislation addresses many of the key issues that need to be included in a comprehensive electricity restructuring bill. However, we believe H.R. 2944 should be modified to establish the necessary ground rules and adjustments required for the transition to competition.

I would like to take a few minutes to discuss, in some detail, the Department's views on four important issues: (1) market power; (2) FERC jurisdiction over transmission; (3) regional transmission operators; and (4) public benefits programs. Thereafter, I will briefly comment on H.R. 2944's treatment of several other items.

Market Power

The primary goal of Federal electricity restructuring legislation must be to aid the transition to competition in a manner that allows consumers to benefit through lower rates. However, significant rate savings can't be achieved if effective competition fails to develop.

Open transmission access and the creation of independent regional transmission organizations should go a long way towards achieving competitive markets. However, access to transmission is, by itself, not enough. Utilities that own substantial amounts of generation in a region or strategically located facilities may be able to raise prices above competitive levels and inhibit the entry of new competitors through horizontal market power. Because electricity markets are becoming increasingly regional and multi-regional, state regulators cannot adequately address market power issues. As a result, it is essential that the Federal government, as the guardian of interstate commerce, be able to take aggressive action during the transition period to ensure that utilities are unable to use horizontal market power to control prices and impede competition.

The antitrust laws are not, by themselves, sufficient to address the market power problems a newly-restructured electricity industry may face. The traditional regime of rate-of-return regulation has led to high concentrations of ownership of generation facilities regulation. As the Department of Justice recently noted in testimony before this Subcommittee:

> The antitrust laws do not outlaw the mere possession of monopoly power that is the result of skill, accident, or a previous regulatory regime. Antitrust remedies are thus not well-suited to address problems of market power in the electric power industry that result from existing high levels of concentration in generation or vertical integration."

FERC currently has the authority to condition merger applications to remedy potential market power. Absent a merger application, FERC's only other available tool to address market power is to deny a request for market-based rates. However, denying such requests could severely impede the Commission's ability to promote wholesale competition.

To ensure that the development of competition is not hindered by the exercise of market power, the Administration's legislation would authorize FERC to remedy concentrations of market power in the wholesale market, including the authority to order the divestiture of assets, if market power is found. In addition, our bill would enable FERC to provide backup market power remedies for the retail market, at the request of a state. This is important because some states seeking to open their markets to retail competition may not have clear statutory authority to remedy market power problems in their state or have jurisdiction over facilities in other states that may be the cause of a market power problem.

Mr. Chairman, we are disappointed that H.R. 2944 fails to address horizontal market power. We recommend that the bill be modified to incorporate the market power provisions in the Administration's bill.

Jurisdiction over Transmission

FERC Orders No. 888 and 889 have had a tremendous positive impact in promoting wholesale competition by requiring jurisdictional utilities to provide competitors access to transmission facilities under rates and terms comparable to those provided to itself. Unfortunately, FERC's open access authority does not directly extend to non-jurisdictional utilities, such as most cooperative and municipal utilities, as well as TVA and the PMAs. The Department supports the provisions in H.R. 2944 which extend FERC's regulatory authority to the transmission facilities owned by previously non-jurisdictional utilities.

We are concerned, however, about FERC's ability to prevent discriminatory transmission access as a result of a recent 8th Circuit Court of Appeals decision—*Northern States Power v. FERC.* In that case, the Court essentially ruled that FERC has no authority to prevent a utility from denying access to others in favor of its own bundled retail sales.

H.R. 2944 states that FERC would have authority only over the unbundled transmission of electricity that is sold at retail, while state regulators would have jurisdiction over transmission when it is part of a bundled retail sale. It is necessary that all transmission owners and all transmission services be subject to similar rules and requirements. The distinction in H.R. 2944, in light of the 8th Circuit decision, would balkanize the regulation of transmission and could have a potentially chaotic impact on the development of competitive markets. FERC would be unable to prevent a utility providing transmission services that are bundled with the retail sale and distribution of power from discriminating against other electricity suppliers in favor of its own generation. State regulators, which would have jurisdiction over

bundled transmission services, may not have sufficient incentives to adequately police a utility's use of its transmission lines, especially if the competing supplier were seeking access to sell power to consumers located in another state.

Mr. Chairman, we urge you to reevaluate this provision. Whether transmission is bundled or unbundled, it is essential to the development of competitive markets that all competitors have non-discriminatory access to the facilities.

Regional Transmission Organizations

Properly sized, independent, regional transmission organizations (RTOs) can provide significant benefits, including the enhancement of reliability and the promotion of more efficient and competitive markets. FERC's recent Notice of Proposed Rulemaking, which encourages transmission-owning utilities to participate in RTOs, is a positive step. However, this voluntary approach does not ensure that appropriate RTOs will be developed.

The Department is encouraged that H.R.2944 would require all transmitting utilities to join RTOs and we generally support the standards for RTO formation laid out in the bill—(1) independence, (2) appropriate scope and regional configuration, (3) operational control over all transmission facilities comprising the RTO, (4) responsibility for planning transmission additions and upgrades, and (5) other standards FERC determines are in the public interest.

We are concerned that the legislation limits FERC's discretion in approving an RTO. While an RTO might meet the standards set out in the legislation, it might very well not be the optimal RTO for a particular region. However, H.R. 2944 would prohibit FERC from disapproving a less-than-optimal proposal as long as the proposed RTO met the statutory standards. In addition, FERC's hands would be tied with regard to RTOs approved prior to the date of enactment. Although a previously approved RTO might require alteration due to changes in circumstances, FERC would be powerless to alter it. In addition, this provision could have a chilling effect on FERC's grants of approvals for new RTOs prior to the date of enactment, if FERC knows that it could not require changes to an RTO following the date of enactment of the legislation.

Moreover, although we support the concept of incentive pricing policies in certain limited situations, it is unclear why FERC should be required to establish a pricing policy designed to encourage transmitting utilities to form RTOs (and extend the policies to already existing RTOs), when the legislation already requires transmitting utilities to join RTOs. It is important to remember that transmission will continue to be a monopoly function. Any deviation from cost-of-service ratemaking should be limited to exceptional circumstances.

Public Benefits

While retail competition has the potential to increase renewable energy's share of the electricity market, the inherent uncertainty of the transition to competition, the recognition of important environmental and energy diversification benefits from renewables, and the fact that existing Public Utility Regulatory Policies Act requirements are incompatible with competition and ineffective under present market conditions suggest that Federal policy towards renewable electricity should be revisited in the context of restructuring.

Mr. Chairman, DOE commends you for recognizing the need to address renewable energy in restructuring legislation. We support the extension of both the Renewable Energy Production Incentive (REPI) program for municipal and cooperative utilities and the wind and biomass tax credits. However, more needs to be done; otherwise, the progress we have made in renewables could be partially lost during the transition to competition because these technologies have not yet achieved cost-competitiveness. The inclusion of a renewable portfolio standard would provide market-based support for the development and deployment of renewable energy technologies. Unlike the mandatory purchase provisions of PURPA, this approach would be consistent with competitive electricity markets.

In addition, we continue to be concerned that retail competition could lead to reduced support for programs that provide important public benefits. Under cost-of-service regulation, programs supporting and promoting research and development, energy efficiency and low-income assistance were supported, in part, through utility rate structures. As utilities prepare for competition, they will be unwilling to include in their rates the cost of programs not included in the rates of their competitors. A public benefits fund, which provides matching funds to the states for low-income

assistance, energy efficiency programs, consumer education and the development and demonstration of emerging, clean technologies, should alleviate these concerns.[2]

Other Issues

Mr. Chairman, while I cannot comment on each and every provision in H.R. 2994, I would like to briefly discuss several additional issues.

- **Target Date/Opt-Out**—Mr. Chairman, the Department recognizes that since Chairman Bliley dropped his insistence on Federally-mandated competition, the debate over restructuring legislation has shifted to other issues. Nevertheless, we continue to believe that there is substantial merit to establishing a target date for the implementation of retail competition and requiring state utility commissions and non-regulated municipal and cooperative utilities to hold proceedings to examine the benefits or costs of adopting retail competition programs. I know we both share the opinion that competition, if it is structured properly, will benefit all classes of consumers. Most, if not all, state utility commissions and non-regulated utilities would likely come to the same conclusion after a thorough examination.
- **Transmission Siting**—We are pleased that H.R. 2944 recognizes that regional solutions to transmission siting issues are both appropriate and necessary. In addition, the Administration has no objections to providing FERC with authority to order transmission-owning utilities to expand their facilities, as long as state siting authority is not diminished.
- **Reliability**—As I discussed earlier, one of the most critical elements of comprehensive electricity restructuring legislation is the need for mandatory reliability standards. The reliability title of H.R. 2944 closely mirrors the language included in the Administration's legislation and language proposed by the North American Electric Reliability Council. We believe the differences between these proposals can be resolved.
- **Consumer Protection**—H.R. 2944 contains several vitally important consumer protection provisions, including items related to information disclosure, consumer privacy and measures designed to prohibit marketers from engaging in slamming and cramming practices. We fully support these provisions.
- **Mergers**—We are pleased that H.R. 2944 retains FERC's authority under Section 203 of the Federal Power Act to review utility mergers and extends FERC's jurisdiction over mergers that involve generation-only and utility holding companies. Utility mergers are not necessarily anti-competitive. However, it is vital that FERC— the regulatory agency with significant experience with and understanding of electricity markets—be able to prohibit or condition a merger that would have a deleterious impact on retail or wholesale competition.[3]
- **Reciprocity**—The Administration believes that each state should have the authority to determine whether to prohibit a utility not fully subject to retail competition requirements from participating as a marketer in that state if the state has implemented retail competition. Recognizing that H.R. 2944 instead imposes a Federal reciprocity requirement, we believe the requirement would be ineffective. By allowing utilities not subject to retail competition to avoid the reciprocity limitation by simply filing an open access plan with a state utility commission, the legislation could very well allow utilities that file sham proposals to escape the intent of the reciprocity provision. We think this provision should be modified.
- **Aggregation**—Mr. Chairman, the Administration commends you for including Section 541 in H.R. 2944. This provision will help entities that are interested in aggregating to increase consumers' purchasing power and enable them to reap the full benefits of retail competition.
- **Interconnection**—We welcome the inclusion of a Federal interconnection standard in H.R. 2944. Distributed power and combined heat and power technologies can enhance both reliability and the environment. We believe a more expansive approach than that included in the bill is required. Interconnection should not be restricted based on ownership or the ability to serve nearby facilities. In addition, we believe that regulatory and tax barriers that inadvertently discourage the use of these technologies should be addressed.
- **Federal Utilities**—We are pleased to see that the key issues associated with Federal utilities which the Administration believes need to be addressed in re-

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[2] The Administration's public benefits fund proposal also includes a rural safety net in the unlikely event that competition adversely impacts rural areas.

[3] To avoid inadvertent impacts on small consumer-owned systems, the Administration bill excludes entities with existing loans made or guaranteed under the Rural Electrification Act from merger review requirements.

structuring legislation, as well as the general approach to resolving these issues, are included in H.R. 2944. Although Title VI of the legislation differs in certain limited respects from the Administration's proposed restructuring legislation, both bills share the same goal—enabling competition to thrive in the regions served by Federal utilities. We believe the differences between the two approaches can be resolved.

- **Private-Use Prohibition**—We agree that it is necessary to resolve the issues surrounding the tax treatment of debt issued by municipal utilities to enable them to fully participate in competitive markets. The small differences between the provisions in H.R. 2944 and the Administration's proposed legislation should be easily bridged.

CONCLUSION

Mr. Chairman, while the states are proceeding with their restructuring programs, all eyes are on Congress to learn what signals the wholesale and retail markets will receive. This Committee's leadership has been essential and will continue to be. Although we do not support H.R. 2944 in its current form, the Administration's approach to comprehensive restructuring legislation has many elements in common with your proposed legislation. And I know that several members of this Subcommittee, on both sides of the aisle, have put forth proposals that merit serious consideration.

We are confident that a bipartisan bill can be reported out of the Subcommittee soon. Secretary Richardson and I, as well as our staff, stand ready to assist you and the other Subcommittee members in this vital endeavor. Only by working together can we take the steps that are necessary to provide consumers with the full benefits of competition.

Mr. BARTON. We thank the gentleman from the Department of Energy for his testimony.

The Chair would recognize himself for 5 minutes for questions.

Mr. Secretary, I would like for you, in your own words, to define market power.

Mr. GLAUTHIER. Market power is the ability of an entity to set prices, to exercise control of the pricing or terms of availability of services in a market.

Mr. BARTON. Okay. I think you are very aware that 24 States have done something on electricity restructuring. Haven't most of those States addressed market power in their State bills?

Mr. GLAUTHIER. Our concern is as we move forward, we feel we need a Federal consistency, a national consistency, and that the Federal Energy Regulatory Commission has some ability to assure that market power isn't used in regional markets, which cross State boundaries.

Mr. BARTON. Okay. Are you—with the exception of the Tennessee Valley Authority and the Bonneville Power Administration, which are Federal utilities that are not at all regulated now by the States, are there any other situation where there is market power concentrated across a region that you are aware of?

I shouldn't let the staff give you the answer, but he is a good guy, so we will let him this time.

Mr. GLAUTHIER. Well, multistate holding companies certainly have control of assets across wide regions.

Mr. BARTON. But there is—I have seen no study that is interstate that indicates, again, with the exception of the Federal utilities, which we do address in our bill, that there is a concentration of market power. And I do see that in every State that has acted, many but not all of those States have addressed market power in some way. So, while I share your concern in the abstract for market power, when we look at the actual market in the United States for electricity, I see no compelling reason to give the Federal Gov-

ernment an authority that it has never had before. Would you like to comment on that?

Mr. GLAUTHIER. Well, we are also talking about a situation of open competition which has never existed before. And what we are asking is that the Federal Energy Regulatory Commission have the authority to ensure that market power is not abused. But we are not expecting that it is going to have to intervene in many cases. This is a question of having the oversight and the ability to ensure that markets will operate.

Mr. BARTON. But the very—and I am not going to belabor this, because we have got a lot of other testimony and a lot of other questioners—but the very intent of the legislation before us is to create competition, to put more players into the market both in terms of having the opportunity to sell and to generate. And you have to assume that there is no public utility commission, no Governor, no State legislature in the country that says, "Yes, we want to concentrate market power for our customers."

I mean, if I didn't think the States and their regulatory bodies weren't cognizant of this potential problem, I would be right with you, but since I have talked to many of them and they are very cognizant of it and very concerned about it, I don't think that we need to put in a Federal market power provision. But having said that, there is one vote for the bill before the committee now, and that is mine, and it takes at least 16 to pass.

Let me go to the RTO provision of the bill pending before the subcommittee. You said some very nice things about our RTO provisions, and I want to thank you. But you expressed a concern that we limit FERC's discretion to force what you call the optimal regional transmission organization. I don't think this is a surprise to you, but that was intentional. We wanted to limit the FERC's discretion, and so my question to you: Why would you assume that five commissioners, as well-informed and well-intentioned as they may be, would have more perfect knowledge than the market participants themselves that are creating the RTO? So long as we require the utilities to participate in an RTO, what is wrong with setting the guidelines? And as long as the participants themselves certify and FERC agrees that they meet those guidelines, why not let them create in their own way, to use your term, the optimum RTO?

Mr. GLAUTHIER. Transmission access I think is going to be one of the greatest keys to success of this program overall. If you don't have open access to transmission, then the rest of the elements of competition are not going to work. The FERC commissioners, while there are five of them, are confirmed by the Senate and do represent the informed perspective of the community. Their ability to look at the patterns that exist in different markets, different regions, we think is important to be able to oversee these regional organizations that will emerge.

Mr. BARTON. Well, my time has expired. I didn't hear you say you thought they would do a better job. So, I ought to quit while I am ahead on that.

We are going to recognize the gentleman from Ohio, Mr. Sawyer, for 5 minutes.

The gentleman from Ohio, Mr. Sawyer, who was here before the gentleman from Illinois and the gentleman from Tennessee, although the gentleman from Ohio did leave, but he did come first.

Mr. SAWYER. I promised you I would come back, Mr. Chairman.kay

Mr. BARTON. Okay, so you are recognized first.

Mr. SAWYER. Thank you. Thank you very much.

Thank you very much for your testimony today and for the obvious depth of thought that you have put into not only the bill that is before us but to a number of the other proposals that are with us today.

If my numbers are right, the current transmission network is somewhere in the neighborhood of 150,000 miles, however you want to measure that. And my understanding is that NERC is anticipating a growth over the next 10 years of some 6,000 additional miles. It seems to me that that substantially understates what likely growth in peak load will be over the next 10 years, particularly if we have the kind of competition for access to transmission that I think we are talking about here. Would you agree that basic assessment?

Mr. GLAUTHIER. Well, I am not sure whether it is miles that will increase or the capacity along many existing routes, but there certainly will be a substantial amount of transmission utilized in this new competitive market.

Mr. SAWYER. Well, let me put it another way. Would you agree that the transmission grid, as it is currently constituted, is constrained?

Mr. GLAUTHIER. Yes.

Mr. SAWYER. And would you agree that it is really not designed to—it was never designed to perform the tasks that it may be called upon to fulfill in a market environment?

Mr. GLAUTHIER. Yes, that is true.

Mr. SAWYER. In that sense, is it your belief that it is even possible to design an optimal template that would fit within what may be determined as existing markets? How would you decide what a market is? How would you call upon the commissioners to choose what a market is?

Mr. GLAUTHIER. We would expect them to look at markets in regional contexts. We think that there will be broad regional patterns, and that is one reason that we encourage the formation of planning mechanisms that would allow planning for new transmission capacity, for example, to be done on a regional basis while still respecting the States' role in selecting individual sites and making those decisions.

Mr. SAWYER. My interest in trying to anticipate what an appropriate Commission role might be is to recognize that the markets that might have been anticipated even 10 years ago are different today from what they would have been 10 years ago had we put such a vehicle in place. And it is almost certain that they will be substantially different from—in 10 years from where they are today.

And it is for that reason that I have real discomfort in talking about putting in place and fixing an optimal design for a regional market that may not even exist as a regional market 10 years from

now, particularly as the technology changes to make possible the continued rapid expansion of what we think of as regions. Would you agree with that?

Mr. GLAUTHIER. Yes. Yes, we would.

Mr. SAWYER. In that sense, then let me ask you: When you say that you support limited incentive pricing policies; that you don't in the sense that you don't understand the need for it if in fact the Commission is in a position to order the formation of RTOs to serve markets that may change substantially even within a span of time as little as 10 years.

Mr. GLAUTHIER. Well, we think there is a need for FERC to have flexibility to oversee this system and to be able to adjust as changes take place.

Mr. SAWYER. Can you tell me why you have more faith in the capacity of FERC to see 10 years down the road than the ability of pricing policies to change to reflect changed demand and changed architecture of a regional market?

Mr. GLAUTHIER. Well, pricing policies will probably drive the proposals that come to FERC. As the planning is taking place within a region, the local and State governments have very strong roles in making those decisions. We do not envision FERC developing a master plan for the country and imposing that, but rather trying to set a set of procedures or rules in place that will help ensure that there is an active process going on everywhere to ensure that this kind of transmission develops.

Mr. SAWYER. Just very briefly, do you see a role for pricing policy in nurturing that growth and evolution?

Mr. GLAUTHIER. We have not built incentives—pricing incentives into our proposals. Our sense is that there will be a strong incentive for development for competitors that want to enter these markets. Whether they need actual pricing incentives to develop this, we have not made a decision. We haven't come to that as an element that we have supported.

Mr. SAWYER. Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Congressman Sawyer.

We recognize the distinguished vice-chairman, Mr. Stearns of Florida, for 5 minutes.

Mr. STEARNS. Thank you, Mr. Chairman.

The administration bill gives FERC extraordinary powers to order divestiture. How many regulatory agencies have the power to completely restructure the industries they regulate, including the power to order divestiture?

Mr. GLAUTHIER. I am not sure how many industries have that. What we are talking about is——

Mr. STEARNS. I don't think you can name one, and yet the administration is giving FERC this extraordinary power. So, I need you to justify it.

Mr. GLAUTHIER. What we are talking about is trying to be sure that there is an independence between the generation assets of a system and the transmission assets, so that a utility not be able to use its position in the transmission market to favor its position with generation; that if we are going to have open competition, we have got to have the transmission system be open to all offers.

Mr. STEARNS. Well, I don't see any precedence for what you are doing here, what the administration is doing. Now, I know you personally probably don't have a big stake in this, but you are here defending the administration's proposal, so I think many of us are just sort of a little dumbstruck here that the administration give FERC so much extraordinary powers, and there is no precedent that I can see to do this. And I don't—I missing something. You are not making the case why FERC has to have these extraordinary powers.

Mr. GLAUTHIER. Certainly we have seen divestitures come from the court system, from the Judiciary in different markets. In this case——

Mr. STEARNS. Yes, but isn't that antitrust law? That is antitrust law. That is not coming from a Government agency.

Mr. GLAUTHIER. Well, in this case what we are dealing with is a set of companies and a whole marketplace which has grown up over decades under a regulatory environment which we are now talking about changing.

Mr. STEARNS. Couldn't the courts do that today?

Mr. GLAUTHIER. We would rather have a planned transition than leave this to the courts. Under today's regulatory environment, where there is a monopoly that is governed or sanctioned by State law, the market power is legitimate; it is appropriate; it has arisen naturally. What we are talking about is trying to change this so that there will be free and open competition in this market.

Mr. STEARNS. Well, staff has pointed out to me that what you are allowing is like if we take, for example, the FAA. They could go in and break up United Airlines or they could go in and break up U.S. Air, and that is the kind of authority that the administration is allowing FERC to have and which you are defending here this morning.

So, we don't see any precedence for it, and we are alarmed that you are giving FERC that power when it really should be to the courts, and so I think our point today, and which it appears we disagree with the administration, is this is an extraordinary power to order divestiture, which we are a little worried about here.

Mr. GLAUTHIER. If I could make one point, and that is that any authority that FERC would have to take those kinds of actions is premised on a determination that there is market power in a particular area that does allow a company to exercise that kind of pricing control in a market. If in fact the utilities take the actions, open up the regions for competition, then those conditions will not exist, and there will not be any ability for FERC to make those kinds of orders.

Mr. STEARNS. Wouldn't you agree that you are establishing a new precedence here? It is like saying the FAA can start to go in and break up airlines and that is a new precedent.

Let me go on here. In your testimony, you have reservations concerning the jurisdiction clarification in section 101. FERC proscribes similar language in Order 888. Why do you disagree with the Commission which has the experience in this area?

Mr. GLAUTHIER. I am not familiar with the section referenced. 101 is——

Mr. STEARNS. Section 101 is to allow FERC to determine all transmission.

Mr. GLAUTHIER. I am sorry, could you repeat the question?

Mr. STEARNS. In your testimony, you have reservations concerning the jurisdiction clarification in section 101. FERC proscribes similar language in Order 888. Why do you disagree with the Commission which has the experience in this area?

Mr. GLAUTHIER. If this is referring to the 8th Circuit Court decision last spring, our legislation was drafted before that decision came out, and since the decision we want to clarify our position here and be sure that FERC would have the authority to guarantee that there is access to the transmission.

As I said in my oral statement, we are not proposing that FERC regulate or decide the rates in bundled transactions but that it be able to have oversight to assure access to those transmission lines.

Mr. STEARNS. Before I give back my time, Mr. Chairman—my time is expired—but basically I think that he is criticizing something that is really not in your bill.

Mr. BARTON. We thank the gentleman from Florida, and we want to thank the distinguished Deputy Secretary for being honest. I couldn't—if somebody said, "What does section 302 of the bill do," I would have to be honest and say I would have to look at the summary before I commented on it. So, we actually appreciate your being honest enough to say, "What does 101 do," although it is the first section in the first title.

The gentleman from Texas, Mr. Hall, is recognized for 5 minutes.

Mr. HALL. You know, Mr. Chairman, it seems to me that one of your renditions or it may have been in one of your letters from the chairman—I am not sure, I saw it somewhere—where you had a carrot out there to those States enticing them in. It seems like the easiest and the surest way and put some type of a structure there that tells them that if they don't take that carrot, they darn well better—should. That is a nice way to treat the States. I think we may resurrect that.

And, Mr. Deputy Secretary, we have a long way to go on this bill, and we are all sitting here with the hard solemn knowledge. The chairman knows it better than anyone that if one senator doesn't like one paragraph in this that they can stop that bill this year, and we are back here the next year. But this is a process we have to move along, and I think the gentleman from Florida, though, got us into the question about restructuring and what the States had done, how many had done it, and how many still need to do it.

My State passed a bill, the State of Texas—I think you are well aware of that—and in the recently passed restructuring legislation down there in Austin, the Texas legislature enacted a generation market power provision that generally required utilities with more than 20 percent of the generation in the State to auction the capacity over the 20 percent threshold for as long as it exceeded 20 percent. That is a mandate or instruction to the State. Do you have an opinion on how that applicable—and how workable that approach would be to Federal laws?

Mr. GLAUTHIER. I don't have a specific opinion on whether we should have that in the Federal law, but in terms of consistency of the Federal statute and that type of a State statute, as long as

the State is taking actions of that sort, then we would not expect FERC would make any finding that there will be a market power situation that would require them to take any additional action at the Federal level.

Mr. HALL. So, it doesn't give you any heartburn at all?

Mr. GLAUTHIER. No, it doesn't.

Mr. HALL. Well, in the event that this subcommittee does not get together—and it is my understanding from the chairman that he would like to pass a bill out. It is also my understanding that he would like to get it as strong a voice to the Chairman Bliley, because he might get another letter back from him if it is not the way—wasn't it in Othello, the merchant of Venice where they said, "Oh, that mine enemy would write me a letter."

Mr. BARTON. I don't think that is germane to the witness.

Mr. HALL. Okay, I will get back.

But in your testimony, you outlined a number of reasons why the Federal Government ought to enact restructuring now, right now, and that is what the chairman is trying to do. I don't know how much of a stonewall he is up against, because we have to navigate the full committee rules of the floor, the Senate, and, there, one person, if they just stand up and make an inquiry, they almost kill any of the bills that are going get over there this late.

So, I guess we have to think in these terms, whether we like to or not. You outlined a number of reasons why we ought to do it, but if we are unable to do it on a comprehensive package in this Congress, what kind of a bare bones package should we enact that probably—that might navigate the Senate? You work both sides.

Mr. GLAUTHIER. The one thing that Secretary Richardson said to me this morning before I came up was, "Urge them to go ahead and act quickly; let us move ahead." We are not prepared to decide where we might fall back. At this point we would like to support comprehensive legislation, work with the full committee to move that ahead.

Mr. HALL. That is a good answer, but be thinking about a fall-back position, because I think it is going to come around.

I yield back my time, Mr. Chairman. I have some other questions, but I will put them in the record and ask that they be—space be left at this structure for my question to go in.

Mr. BARTON. I thank the gentleman from Texas, and I would make the point before we recognize Mr. Largent, it goes back to something that I said. The Chair, and I think the members of the subcommittee, share the administration's concern about perceived market power, but we are simply unconvinced that the States don't share that concern, and the States that have acted in different ways have addressed market power. California required divestiture; Texas did not; Pennsylvania did not, but they are addressing it.

So, there is not a need for a Federal one-size-fits-all on the States that have yet to act. If the States that have acted have addressed it, why do we think that the States that have not yet acted but might, if we pass a Federal bill eliminating the barriers, would not address it themselves? Before I recognize Mr. Largent, do you want to——

Mr. GLAUTHIER. If I may, if adjacent States, for example, have not acted, then even though your own States has taken actions, the market there may be impacted; it may not really be the opportunity to get the advantages of competition. If the States have acted, then the sorts of authorities we are talking about for FERC would not have any effect, because there wouldn't be any remaining problem for them to have to act about.

Mr. BARTON. Okay. The gentleman from Oklahoma, Mr. Largent, is recognized for 5 minutes.

Mr. LARGENT. Mr. Glauthier, let me ask you a follow-up question to the chairman's remarks. What authority would a State have to mitigate market power that existed across its State border? In other words, generation facilities that are of the same company that cross State lines, what ability would one State have to mitigate that market power that existed across its border?

Mr. GLAUTHIER. That is an excellent example, and that is one of the concerns we have; that it seems the State's authority stops at its State border.

Mr. LARGENT. But electricity does not stop at the State border, is that correct?

Mr. GLAUTHIER. That is absolutely correct.

Mr. LARGENT. Which is why we are here today.

Let me—in your testimony, on pages—the bottom of page 6 and the top of page 7, you are talking about "as a result, it is essential that the Federal Government, as the guardian of interstate commerce, be able to take aggressive action during the transition period to ensure that utilities are unable to use horizontal market power to control prices and impede competition." When you say "during the transition period," what kind of period of time are you talking about?

Mr. GLAUTHIER. We are not sure how long it will take to transition into a fully competitive working market. Certainly, the first few years we expect there will be some bumps in the road, and maybe some transitional actions will be required that would not have to be long-term actions. Some of our provisions go for 10 to 15 years in our bill. It really will depend, whether you are talking about things that require capital investments and take some time or whether they are more operating changes that can phased in rather quickly.

Mr. LARGENT. So, one of the ideas that I floated before the hearing—just throw out right now—is that I think most experts would say the transition period would be somewhere between 3 and 5 years to get to a fully competitive market. Is it possible to institute some sort of market power tools, placed in FERC hands, that would sunset after a certain period of time, as we have gotten into a more competitive market?

Mr. GLAUTHIER. I think the concept is a concept that is good that we ought to work with a bit. Whether the exact period would differ, for example, for different kinds of actions, such as the planning and action process in investing in new transmission facilities, which will take some time, might differ from those actions that focus on the market and the behavior for pricing and offerings in a particular market or electricity for retail customers. But I think the idea is a good idea, and we ought to take that into consideration.

Mr. LARGENT. Well, one of the market power tools that the administration proposes, that, frankly, I am not a fan of, is the ability to order divestiture. But one comment I would make about that, one of my colleagues earlier, Mr. Stearns, mentioned, or tried to make the comparison between FAA being able to order divestiture of United Airlines or American Airlines and trying to compare that with FERC ordering divestiture of the Southern Company. That is hardly comparing apples to apples since the Southern Company, other IOUs, have been granted a monopoly status, whereas American Airlines and United have not. So, I don't think that is a fair comparison.

But I want to go on down on page 7 in your testimony. You talk about FERC's only other available tool—this is to address market power and wholesale markets—is to deny a request for market-based rates. Now, many people, before FERC had Order 888, suggested that there could be market power existing in the wholesale market, and so FERC needed to have a tool at its disposal to address market power and wholesale, and one of them was to deny market-based rates; in other words, stay with the cost-based rates and deny market-based rates. Has the FERC ever utilized that tool in its history since Order 888? Have they ever denied market-based rates as a result of market power?

Mr. GLAUTHIER. I don't believe they have since 888, but you may have to ask that question again to the next panel——

Mr. LARGENT. Okay.

Mr. GLAUTHIER. [continuing] to get a definite answer.

Mr. LARGENT. Thank you.

My last question, Mr. Chairman, goes back to the Public Benefits Fund. You make a case for the administration's position on the Public Benefits Fund. Twenty-four States have already moved and done something, including Oklahoma, on deregulation. Have all 24 States addressed the Public Benefits Fund?

Mr. GLAUTHIER. No, not all of them have, and there has been some variety among those who have—different lengths of time, for example, that a Public Benefit Fund would exist. So, we think it is important to have one that would be consistent and applicable across the country.

Mr. LARGENT. Okay. Thank you, Mr. Chairman. I yield back.

Mr. BARTON. I am sorry, Mr. Largent. I was engaged in a staff conversation. You yielded back your time, all right.

The gentleman from Illinois, Mr. Rush, is recognized for 5 minutes.

Mr. RUSH. Thank you, Mr. Chairman.

Mr. Deputy Secretary, I want to commend you on your testimony and answers to the questions this morning. I think you have been very forthright and illuminating in terms of the administration's position.

H.R. 2944 repeals PURPA without establishing renewable energy portfolio standards. However, the bill does provide for tax incentives regarding the use of renewable energy. In your opinion, which provision would generate the greatest amount of competition while also acting as the greatest incentive for the use of renewable energy?

Mr. GLAUTHIER. We favor a renewable portfolio standard; think that that provides the support for these not yet fully mature technologies that are going to be increasingly important in our electricity sector. We also support the tax incentives and would like to see both implemented.

Mr. RUSH. Section 542 of the bill will give FERC jurisdiction over distributed generation facilities, which are defined as electric power generation facilities of 50 megawatts or less. Such FERC authority appears to be a departure from previously established jurisdiction boundaries, and they seem to be in contradiction to section 101 of the bill. Might this provision be seen as a preemption of State authority?

Mr. GLAUTHIER. I believe the authority for the distributed power is really to be sure that there is the ability to look at the systems as an integrated system and to incorporate all of the power that would be in a market.

Mr. RUSH. Well, let me ask, are there any other areas regarding distribution reliability where FERC jurisdiction would be appropriate?

Mr. GLAUTHIER. The local distribution systems are not under the authority of FERC. So, FERC's authority would really stop when the power ends the transmission—long-term transmission system and enters the local distribution utility.

Mr. RUSH. So, in answer to the question then, there aren't any areas regarding distribution reliability where FERC jurisdiction would be more appropriate or that will allow FERC to address issues of reliability.

Mr. GLAUTHIER. I don't believe there are. I think you are right.

Mr. RUSH. Do you think that this is an appropriate——

Mr. GLAUTHIER. We think that it is important for the States to deal with this, so we are having a meeting, a regional meeting, in the Midwest, in Chicago, at the end of this week.

Mr. RUSH. Yes, I am supposed to testify. I will be a part of that meeting on Friday.

Mr. GLAUTHIER. So, we are looking forward to try to deal with that and to get more ideas developed in that area.

Mr. RUSH. Are you concerned about the epidemic of blackouts that occurred over the summer?

Mr. GLAUTHIER. We are concerned about that, and Secretary Richardson this summer announced a six-point plan to try to deal with that.

Mr. RUSH. And so you are—the position of DOE right now is we still want to leave it at the—leave this issue of reliability at the State level without any Federal intervention at all, any Federal guidelines or standards?

Mr. GLAUTHIER. No, I am sorry, I didn't mean to leave that impression.

Mr. RUSH. Please don't.

Mr. GLAUTHIER. Reliability is one of the primary reasons we feel there is a need for Federal legislation, and that we need to move from what is today a set of voluntary standards on reliability to a set of mandatory standards across the country. As we see deregulation or increased competition occur, we are going to see more and more participants in the market at all levels. It is going to be more

important to have a uniform and enforceable set of reliability standards for the industry.

Mr. RUSH. Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Congressman Rush.

It seems like we recognize the gentlemen from Illinois in conjunction. So, this time we go from the democratic gentleman from Illinois to the republican gentleman from Illinois, Mr. Shimkus, for 5 minutes.

Mr. SHIMKUS. The dynamic duo of the committee, Mr. Chairman.

Mr. BARTON. That is right.

Mr. SHIMKUS. I am pleased to follow my colleague from Chicago.

It is great to have you here, and I think we are focusing on a major concern based on the administration's bill. We know that there are no market power provisions in H.R. 2944 other than the RTOs, because the hearing record seems to have been made that they clearly are not necessary, if you have sat in all the hearings that we have had.

My State addressed market power through a mandatory ISO. How would you think my State would feel if a restructuring bill was passed, signed into law, that then took away their authority based upon FERC's power in determining market power?

Mr. GLAUTHIER. Well, I think if the State authority has acted to really assure that there is competition occurring——

Mr. SHIMKUS. Well, wait—really assure? What do you mean by "really assure?" I mean, based—the dilemma we have here is you trust the Federal regulators; I trust my public utility commission. Now, I guess the question is, is that your position? Do you trust the Federal regulators over the State public utility commission?

Mr. GLAUTHIER. We look to the State commissions to act first and to try to incorporate the programs that they have already decided to put in place, in many cases, or that States will be deciding to put in place, and we are looking to FERC to have an oversight authority to guarantee that as the States act we don't end up with a patchwork of programs that are inconsistent or where some——

Mr. SHIMKUS. Tell me why the administration's position is willing to destroy the deregulation bill in the States of Illinois based on superimposing FERC regulation with respect to ISOs and market power? Why are you willing to give up a State that has moved to address all these concerns addressed in a deregulatory bill based upon the assumption that the RTOs, or in this case a mandatory ISO, will not address the concern of market power?

Mr. GLAUTHIER. Well, first, I don't agree with the premise that we are going to change the State program.

Mr. SHIMKUS. Well, it does, though, in Illinois. It will cause the players to then claim that the rules have been changed, and based upon that rule they can go and have this law dismissed.

Mr. LARGENT. Would the gentleman yield just for a second?

Mr. SHIMKUS. The gentleman will yield.

Mr. LARGENT. I don't want to defend the administration's position—he can do it himself—but I believe in the administration's bill that the only time the FERC would come in would be at the request of the State of Illinois. The State of Illinois would have to petition the FERC to come in and to look at unmitigated market power.

Mr. SHIMKUS. Well, we are going to see if that is the administration's position.

Mr. BARTON. We appreciate the gentleman from Oklahoma defending the administration's position. This is truly bipartisan and bicameral process.

Mr. SHIMKUS. Well, I don't have an answer, first.

Mr. GLAUTHIER. Well, part of the answer I wanted to give is that——

Mr. LARGENT. Well, isn't Mr. Largent correct in defending the administration?

Mr. GLAUTHIER. Yes, he is. Yes, and we appreciate the assistance.

In market power, that is the State would have to make the petition.

Mr. SHIMKUS. But has the administration addressed—asked my public utility commission? I mean, in promoting the Federal—in the administration bill, have you raised this to the public utility commissions of the various States?

Mr. GLAUTHIER. There certainly have been conversations with the——

Mr. SHIMKUS. The State of Illinois?

Mr. GLAUTHIER. Well, with NARUC. I am not sure that the——

Mr. SHIMKUS. Yes, or no; State of Illinois?

Mr. GLAUTHIER. I can't guarantee that.

Mr. SHIMKUS. Okay. I think—okay. Do you have anything else that you want to add.

Mr. GLAUTHIER. I just wanted to make the statement that the requirements we are talking about are intended not to replace the State actions but to follow on. If the States' actions for some reason are not termed sufficient—and I understand the concern you have about who makes the decision——

Mr. SHIMKUS. And my time is expired. I will just say that the State of Illinois went through a very tedious process to move to competition, and as people know on this committee that I am going to be guarded to make sure that the work done in the State of Illinois is not tubed by any interests, either interstate or intrastate.

So, with that, I yield back my time, Mr. Chairman.

Mr. BARTON. All right. They are not called the Fighting Illini for nothing, Mr. Secretary. Mr. Shimkus is stalwart in his defense of the State of Illinois, just stalwart.

We would recognize the gentleman from Massachusetts, Mr. Markey, for 5 minutes.

Mr. MARKEY. Thank you, Mr. Chairman, very much.

And we are operating obviously in terrain that has been trod before—divestiture authority is well established as a Federal power. Obviously, the Department of Justice, under antitrust laws can force divestiture, and the Federal Trade Commission, under antitrust laws, can force divestiture. The Nuclear Regulatory Commission, under the Atomic Energy Act, can force divestiture. The Securities Exchange Commission, under PUHCA, can force divestiture. So, this is—not only is it not unprecedented, it is deeply woven into the fabric of the relationship between the Federal Government and the States.

So, Mr. Secretary, I would like to ask you to very specifically, looking at the Barton bill on FERC jurisdiction over the transmission system, what will happen to the transmission system and energy market if section 101 of the Barton bill is enacted?

Mr. GLAUTHIER. Our concern is that the transmission systems, the regional systems, may develop in a pattern that is not optimal for individual markets, and we want the FERC to have the responsibility to oversee that, be sure that in fact the open access, that is the objective of full competition, will be available.

Mr. MARKEY. Are you familiar with the market concentration provisions of the Texas law and whether it could serve as a model for the Federal law?

Mr. GLAUTHIER. I am not personally familiar with the details of it.

Mr. MARKEY. Do you think it makes sense for the Federal law to be weaker than the Texas law?

Mr. GLAUTHIER. No, in principle, I don't.

Mr. MARKEY. Do you think that—do you believe that transmission owners will form adequate RTOs without clear FERC authority?

Mr. GLAUTHIER. No.

Mr. MARKEY. What do you think about incentive transmission pricing? Why do transmitting utilities need incentives to join RTOs when some already are in RTOs, and the bill already requires those that are not in one to join one?

Mr. GLAUTHIER. We are not sure that there is any incentive needed for that. We have not proposed an incentive of that sort.

Mr. MARKEY. Do you think that—so, you should believe that the RTOs should have open membership requirements?

Mr. GLAUTHIER. Yes, we do.

Mr. MARKEY. You do. Are you concerned about the prospects for utilities to favor their own generation in interconnection to the transmission system?

Mr. GLAUTHIER. Yes, we are.

Mr. MARKEY. Do you think that we need interconnection language in the Barton bill in order to ensure that we can prevent against such activities by utilities?

Mr. GLAUTHIER. Yes, similar to what we have in the administration bill.

Mr. MARKEY. Now, Chairman Hoecker points out in his testimony that the Barton bill actually would prevent FERC from ordering transmitting utilities in Texas to provide open access to their transmission systems. Do you share his concerns about this type of exemption?

Mr. GLAUTHIER. I am, as I said, not specific with the details with the Texas one, but we do share his concerns in general about this area.

Mr. MARKEY. Do you think that we should welcome Texas into the Union?

In terms of the electricity restructuring debate, it is understandable that Alaska would argue that it is not one of the 48 contiguous States as you try to construct a national model. My objective, ultimately, is to make sure that all of the lower 48 are included and that this national market too be.

And, finally, Mr. Chairman—Mr. Secretary, if we were to grant FERC market power authority but then sunset that authority in 5 years, couldn't the incumbent utility monopolists sue to block competition from coming and then run the clock out until FERC couldn't use its market power authority?

Mr. GLAUTHIER. I think we would have to look very carefully at any possible transition rule so that there isn't potential for abuse.

Mr. MARKEY. Thank you, Mr. Chairman.

Mr. BARTON. Thank the gentleman.

We recognize the gentleman from North Carolina, Mr. Burr, for 5 minutes.

Mr. BURR. Thank you, Mr. Chairman. I learned a lot in that last exchange out of all the times that we have been through debates on electricity.

I think I finally figured out where my good friend, Mr. Markey, is. He is in a touch pinch in New England, because he needs lower prices. He just doesn't want to let the marketplace do it. He would like it to be mandated that you have lower prices regardless of what the cost of generation. Regardless of where you get it from, let us just make sure that everybody absorbs the cost of the problem in New England. Let us create another problem everywhere.

And there is a real important key to it—you have to have a Federal regulator to accomplish it. It does not happen with State regulators. You can't link it together, and I am not so sure that that is not where the administration is also.

Let me ask you: Define competition for me.

Mr. GLAUTHIER. Competition, in my view, is the offering of products or services at availabilities and prices where the consumers are able to make their selection, where there is an opportunity to choose among those competing——

Mr. BURR. So, choice is a very important thing for competition.

Mr. GLAUTHIER. Yes, sir.

Mr. BURR. And is more choice better than less choice?

Mr. GLAUTHIER. Yes.

Mr. BURR. And is competition good?

Mr. GLAUTHIER. Yes, it is.

Mr. BURR. Is choice good?

Mr. GLAUTHIER. Yes.

Mr. BURR. Tell me about consumers in Tennessee? Do they have choice?

Mr. GLAUTHIER. Not currently.

Mr. BURR. Should they?

Mr. GLAUTHIER. That is a part of our proposal and a part of this bill, as well.

Mr. BURR. And how much choice will they have?

Mr. GLAUTHIER. Well, it is going to be up to the individual municipal utility systems or the coops to decide whether they want to participate under our bill.

Mr. BURR. What would be an abuse of market power? You talked about the abuses to market power. Tell me what one of those abuses would be?

Mr. GLAUTHIER. Well, one abuse would be if a utility in a region is able to dominate the local systems——

Mr. BURR. So—and I don't want to interrupt you—but if you have competition by your definition, which is choice, you can't have abuse of market power, can you?

Mr. GLAUTHIER. If you are really offering choices, that is right; if there is the opportunity for choice. That is what we are trying guarantee.

Mr. BURR. So, the only way to have an abuse of market power is if you have an instrument that stands in the way of choice in the marketplace.

Mr. GLAUTHIER. An instrument or an ownership pattern or some of other control that does it.

Mr. BURR. Now, would that control be excessive regulatory authority by the FERC?

Mr. GLAUTHIER. We think that that is a technique to try to help assure that we don't have the kind of control that we are worried about. We worried about——

Mr. BURR. Give me an instance where a Federal regulatory agency encouraged and created competition versus stymied and destroyed competition.

Mr. GLAUTHIER. The Department of Justice and the Federal Trade Commission, of course, are doing this all the time.

Mr. BURR. Now, would they be a good one to put in charge of merger?

Mr. GLAUTHIER. We think that FERC has a degree of technical expertise in understanding this market that puts them in the appropriate role here.

Mr. BURR. So, in every case but this one, they would be the correct authority.

Well, I thank you for your answers. Mr. Chairman, I yield back.

Mr. BARTON. The Chair would recognize the gentlelady from Missouri, if she is ready, or we can go to another Republican and then when you are ready come to you. Are you—do you want some time? Okay.

Then we recognize the gentlelady from New Mexico, Congresswoman Wilson, for 5 minutes.

Ms. WILSON. Thank you, Mr. Chairman.

I wanted to ask you some questions related, really, to a statement in your testimony. You say, "What we do at the Federal level and when we do it will have a profound impact on the success of State and local retail competition programs." And the questions I have really have to do with how we make this transition from regulated to market-driven power, and, as you know, the Department of Energy not only deals with this as a policy issue but as a consumer in my State of New Mexico.

The Department of Energy is actually one of the largest industrial users of power in Albuquerque, New Mexico, because you control the contracts for Kirkland Air Force Base. And for those of you who aren't aware of it, Kirkland uses about 65 megawatts of power in New Mexico. It is one of the largest industrial users, and that, to put it in context, is the city of Santa Fe, our capital city, uses, on average, about 88 megawatts of power. We are talking about a large industrial user.

The Department of Energy has applied to move to market power for Kirkland Air Force Base immediately even though State law,

passed by the State legislature, says that we are going to transition to that starting with retail consumers and small businesses and just individual customers in 2001 and industrial consumers in 2002 so that we don't shift costs from large industrial users to schools and individual users and small businesses.

Is it the Department of Energy's position that you can enter a competitive marketplace before every other industrial user in the State of New Mexico?

Mr. GLAUTHIER. My understanding is that the contract you are discussing is a wholesale contract, and our application to FERC follows the procedures for that. We do want to be sure that our actions follow the appropriate actions for all entities there.

Ms. WILSON. There is a Federal law that also says Federal agencies must comply with State law and that no Federal appropriation, whether through the Department of Defense or the Department of Energy, can be used outside of the context of State law, which prohibits industrial users from going to market power until 2002. Is it the Department of Energy's position that this law doesn't apply?

Mr. GLAUTHIER. No, it is not. It is my understanding that that law applies to retail sales again, and we certainly want to be sure that we are doing everything within the confines of the law and appropriate policy.

Ms. WILSON. Is it your position then that you are not an industrial user?

Mr. GLAUTHIER. My understanding is this is a wholesale contract and not an industrial, retail contract with public service in New Mexico.

Ms. WILSON. And since it is a wholesale contract, what you are saying is that the State law passed in 1999 does not apply to you.

Mr. GLAUTHIER. This is a different category than retail sales.

Ms. WILSON. New Mexico is going to competitive market power in a phased way—2001 for retail, 2002 for large industrial users. Is it your position, then, that the Department of Energy is neither of those?

Mr. GLAUTHIER. That is my understanding; that we are a wholesale customer and so do not fall within those groups.

Ms. WILSON. And, so you don't have to comply with any of the State law passed in 1999?

Mr. GLAUTHIER. What we are trying to do is to move toward competition and to do it within the prescriptions that apply to wholesale sale. So, that act does not apply.

Ms. WILSON. So, the circumstance then is that the largest industrial user of power in the State of New Mexico is the Department of Energy and that you feel you are not covered by State law. Is this then going to be the position of the Department of Energy or of the administration on every other Federal Government user of power as we move to retail competition in the States?

Mr. GLAUTHIER. I think our position will be that we have to adhere to all of the appropriate laws and policies that relate to whatever categories our contracts fall under. In this case, it is a wholesale sale. I don't know what the other categories or other situations would be.

Ms. WILSON. Thank you, Mr. Chairman.

Mr. BARTON. The Chair wants to let the gentlelady know the subcommittee's on the side of the schoolchildren and the small consumers in the great State of New Mexico, and I bet we will get the administration to be on that same side. I just have a feeling since Secretary Richardson used to represent New Mexico that we can work that problem out. I think we can.

Does the gentlelady from Missouri wish to be recognized now?

Ms. MCCARTHY. I thank you, Mr. Chairman, very much for your indulgence, and I apologize to the panelist for missing his testimony. My State of Missouri's campaign finance law was before the Supreme Court, and I, having advocated for campaign finance reform while a State legislator and now again in the Congress, felt compelled to be there.

But with 24 States in some stage of deregulation of electric energy, including my own, what has DOE seen as a successful model of deregulation, and what—would you please share with us what you—to what you—what attributes are in a success model for any State?

Mr. GLAUTHIER. I don't believe we have actually pointed to any individual State and said ''This is the example.'' What we see are elements in the patterns across the country which are strong and constructive steps toward competition and toward opening up these markets. We like to encourage the States to take actions that seem appropriate to them and be sure that the overall pattern is moving forward.

Ms. MCCARTHY. Then it sounds like you are quite willing to let States proceed to devise their own models of deregulation and have a kind of a hands-off approach until perhaps all States have completed that task, then take a step back and decide what role the Federal Government has at all in this process, if any.

Mr. GLAUTHIER. We would like to encourage the States to develop their own plans and programs, and what we want to do is be sure that there is an appropriate Federal oversight authority to step in if needed in those selected cases.

Ms. MCCARTHY. And at what date out in the future would you want that authority?

Mr. GLAUTHIER. The way we have introduced our bill it would be to ask each State to make a formal decision by 2003——

Ms. MCCARTHY. No, no, that is not my question, but perhaps you are getting to the answer; I apologize if I interrupted. But I don't see a role for you now at all. I think States are perking along and doing just fine. Now, there is no one perfect model yet, but, as you indicated in your answer to me, eventually we would be able to take a look at what works well for the States or regions or applications.

But I guess the real thrust of my question is why do we need you involved at all in this? I think that is what I need to hear, and if you have already answered that a dozen times before I got here, I apologize; just be succinct. And at what point do you need to be engaged? I don't believe you need to be engaged at this point at all. But is there sometime out there, perhaps if the States don't work cooperatively as a region or as groups, that you would need to be engaged?

Mr. GLAUTHIER. I think one example would be the transmission access area where if States are moving toward competition themselves, but there are inconsistencies among States within a region and a concern that some utilities are not getting access to the transmission facilities in a neighboring State to be able to sell to customers, then that kind of action is the sort of thing we think that FERC should have the authority to look at to see whether any additional steps are needed. That could happen soon. That could happen early as some States move ahead to implement their programs.

Ms. MCCARTHY. So, at what point, then, do you want FERC engaged in this process? Only at the point when States can't get along?

Mr. GLAUTHIER. We would like FERC to have the authority now to begin to oversee the way these programs are being implemented and think that it will be important to have them involved from the beginning.

Ms. MCCARTHY. Would you explain what you mean by involved, because I think that is where some of this cooperation breaks down? I think there is a fear that you—that FERC will come in and try to tell States what to do when States are out there doing what they know best and think is right. And I don't want to be a party to some confrontation that isn't necessary.

Mr. GLAUTHIER. A couple of examples. One would be in the reliability area. We think there is a need for reliability standards that would be developed and enforced nationally. That ought to start now. It ought to begin as we are seeing this market bring in more and more——

Ms. MCCARTHY. But haven't we been doing that?

Mr. GLAUTHIER. We have voluntary standards right now. There are no mandatory reliability standards.

Ms. MCCARTHY. Why do we need mandatory ones, if the voluntary ones are working. Is there a problem?

Mr. GLAUTHIER. Yes, we think there is a problem. This summer, for example, the power outages certainly demonstrated some kinds of problems. As we see markets open up, we will have more and more entrants, more diversified kinds of companies offering services in generation and transmission and then local distribution. All of that is going to increase the uncertainty of the reliability, and we need to be sure that we have got the ability to keep the lights on and make sure everyone is getting the services that they deserve.

Ms. MCCARTHY. Don't you think that the public service commissioners, or whatever they are called in the respective States, also feel that way?

Mr. GLAUTHIER. Yes, and we actually would think they would encourage this; that the reliability standards are something I believe they support.

Ms. MCCARTHY. Why do they need you, if that is the case?

Mr. GLAUTHIER. A lot of it is on an interstate basis. It is not within any single State, and so you really have large regions of the country interconnected in a way that has to be overseen more broadly.

Ms. MCCARTHY. We are doing that now in many parts of this great Nation. I live in Missouri; I get my energy from Kansas. It seems to work just fine. I guess I am hoping that we engage you in a role where you actually are problem-solving but not creating problems, because I happen to think it is working very well out there. We have got wonderful rates in the Midwest, and there aren't a whole lot of people complaining about it.

Mr. GLAUTHIER. In the reliability area, for example, our expectation would be that the organization would grow out of what we have now with the National Electric Reliability Council; that it would have a strong role of the States; that it would not be at war with the States, but rather would be a way for States to participate together and help set these standards and be sure that they are in place in a way that everyone who participates in the market really has to follow.

Ms. MCCARTHY. I thank you. I very much appreciate those thoughts, and I appreciate what you are saying, and I welcome that. I wanted to hear that this was going to be cooperation with States that are already out there doing it, not a Federal imposition of how to do it, but yet a partner in making sure that the customer is well served.

And, Mr. Chairman, I apologize for going over my time limit.

Mr. BARTON. No, ma'am, we were delighted to have you go over your time, because you echoed much of what I said. I don't want to spook you, but it sounded—it was like gentle rain on the plain in the spring to hear your thoughts. So, we appreciate that very much. We will be happy to add you as an original co-sponsor; in fact, the only co-sponsor of the bill.

We recognize the gentleman who represents the top 20 undefeated Mississippi State Bulldogs for 5 minutes for questions.

Mr. PICKERING. Thank you, Mr. Chairman, and I want to commend your efforts in putting this legislation together and having this hearing today. And in a spiritual sense, "Blessed are the peacemakers in the legislative context." Too often it is "Blessed are the peacemakers for they have all been shot." And I hope that is not the case here, as we try to compete—I mean, balance a competing interest in the regions and look at the issues.

I am going to take a little bit of a different tack than the other members. I am actually going to ask questions as it relates to the legislation.

Mr. Secretary, in H.R 2944, the subcommittee chairman's legislation, he amended section 203 of the Federal Power Act to expand FERC reviews of sale of power plants and transmission facilities by State and municipal utilities, cooperatives, and Federal electric utilities. Now, why he expands that authority, he also limits the time to 90 days of that review. What is your view, your opinion, of that? Is it necessary to expand the authority into those other areas? Do you support that? And what is your view of limiting the time?

Mr. GLAUTHIER. We do support the expansion into these other utilities that have been non-jurisdictional utilities. On the timeframe, I would like to defer to the next panel and ask them. We think that it is certainly important to be sure that the decisions

can be made with enough information in front of them, and I don't want to presume that or speak for them.

Mr. PICKERING. Well, why is there a need for Federal review of these sales into, for example, cooperatives or municipal utilities? Could we not maintain under current jurisdiction with the timetable to assure a timely review and decision with a certainty of markets as we go into this transition? Why do you need to go into these other areas where FERC currently has no jurisdiction?

Mr. GLAUTHIER. Our feeling is that we need to be sure that the access and market power issues can be addressed—the ones we have been discussing for some time this morning—that all utilities in the market really have to be following the same guidelines, the same rules. So, having them all a part of the same system will be important.

Mr. PICKERING. Do you see the potential for a municipality or a cooperative to have market power?

Mr. GLAUTHIER. In certain areas, there are large coops, there are—there is the possibility.

Mr. PICKERING. Another question deals with mandatory RTOs. Now, FERC is going forward in its NOPR based on an incentive-based approach, non-mandatory approach. Do you favor a mandatory RTO or incentive-based approach to achieve the type of transmission organization necessary to promote competition?

Mr. GLAUTHIER. We think that the utilities will want to join RTOs. I don't believe there is a need to provide strong incentives or the type we talked about earlier that is in this bill. In terms of mandatory RTOs, I personally doubt that there will many occasions where utilities have to be directed to join an RTO. I think that it is more important that we have the FERC involved in overseeing RTOs to be sure that they are appropriately sized for the regions that they are dealing with; that there is a rate structure.

Mr. PICKERING. So, are you saying that a mandate is not necessary? Incentives would be sufficient with FERC participation, cooperation, counsel?

Mr. GLAUTHIER. I think a mandate is necessary as a fall-back, but that it will not be operative very often; that, in fact, utilities will come forward and join RTOs, but I think you need a mandate there as a guarantee for some small percentage of systems.

Mr. PICKERING. Let me give you another example of whether mandatory—a mandate is necessary or not. In telecommunications—which I realize is different, but there are some parallels—we gave an incentive approach for local phone companies to open their markets and in return if they opened their markets, they could get into long distance—a non-mandatory approach but an incentive-based—if you do this, you will receive freedom to go into other markets. Bell Atlantic is about to petition to open its market in New York and other regional companies are preparing to do that.

As the market forces and the convergence, as well as the consolidation of that market takes place, it seems to be that both regulatory incentives and market pressures are achieving the objectives without a mandate. Now, if that is the case in telecommunications, why would that not be the case in electric utilities?

Mr. GLAUTHIER. Congressman, I am not sure I understand the example exactly, because a few years ago with the break-up of AT&T, you seemed to have the break between local distribution and long distance, which is somewhat similar to our local distribution utilities and the transmission.

Mr. PICKERING. So, if you put in the open access requirements, if you eliminated the vertical integration issues of market power and you gave incentives to do so with reliability and transmission organizations that would be appropriate, do you need mandates?

Mr. GLAUTHIER. Well, the mandate I think in this industry is the parallel to the court order. The reason that it is a mandate we are talking about for the transmission——

Mr. PICKERING. But you are confusing long distance with what we did in local. The legislation was different than what the AT&T consent decree did.

Mr. GLAUTHIER. Yes, but I believe what we are talking about here is really a requirement to be sure that the transmission access is available to everybody; that transmission is not being used as a point of leverage with generation assets alike, and so to guarantee that transmission assets are independent and available to everybody there does need to be some requirement.

Mr. PICKERING. Mr. Chairman, I know my time is up. Could I have one additional question? And this deals with the reciprocity clause and the chairman's legislation. Are you familiar with that?

Mr. GLAUTHIER. Yes, I am.

Mr. PICKERING. And what are your views of the reciprocity clause in the proposed legislation? Do you support it, oppose it? Is there a way to improve it? And should it be State-specific rather than broadly based?

Mr. GLAUTHIER. It is important to have the clause. We do support the reciprocity clause, and it needs to be able to be used on an interstate basis so that if a utility in one State has its market opened up to competition, it is going to be able to compete in the markets with those utilities that are trying to enter its market. That may cross State bounds.

Mr. PICKERING. But as far as the specific legislation proposed, do you support the reciprocity language or would you narrow it to make it on a State-by-State basis?

Mr. GLAUTHIER. The——

Mr. PICKERING. If you understand my question. If I need to clarify or ask a better question, I can try.

Mr. GLAUTHIER. Well, the position in our own legislation is that the State would make the decision on reciprocity, and I think that that clarifies my response.

Mr. PICKERING. The Barton proposal would require every utility, if they have assets in other States that are open, if they have a closed State, to submit a petition in support of competition in the State that is closed before their facilities in other States could participate in an open, competitive market. Do you support or oppose that approach?

Mr. GLAUTHIER. Okay, our approach is to support giving the States the discretion and not the Federal Government the authority over that.

Mr. PICKERING. I think I understand your position. Thank you, sir.

Mr. Chairman.

Mr. BARTON. We thank you, Congressman Pickering.

Deputy Secretary Glauthier, we will have other written questions for you, but there are no other members present that have not had an opportunity to ask at least oral questions. So, we are going to excuse you. We appreciate your presence today. We want to commend you and the Department—oh, whoa, I didn't see Mr. Bryant; I am sorry.

Mr. BRYANT. Well, now that you have recognized me, I will——

Mr. BARTON. I am sorry, Congressman Bryant.

Mr. BRYANT. Let me just ask, if I could——

Mr. BARTON. Five minutes.

Mr. BRYANT. [continuing] just a couple of questions in regard to some environmental issues. The administration bill and the Pallone bill set a Federal renewable portfolio standard of 7.5 percent by the year 2010. Is that realistic?

Mr. GLAUTHIER. Yes, we think it is.

Mr. BRYANT. A number of the States already have established their own individual standards in this area. Is there a need to clarify State authority to impose renewable portfolio standards?

Mr. GLAUTHIER. We think there is a need for a national standard, and what we proposed is one that would have trading credits, if you will, so that if a State, one area, can build renewable capacity more easily than another, more competitively, then it can be done there, and the overall requirement can be met. And, so it would not have to met State-by-State; that is, physically, by assets in each State.

Mr. BARTON. Would the—could the gentleman from Tennessee yield?

Mr. BRYANT. I would be happy to yield.

Mr. BARTON. You answered Congressman Bryant that the 7.5 percent mandated renewable was realistic, but my staff just told me in order to meet that target by the year 2010, 50 percent of all new generation that is built between now and then would have to be renewable. Do you really think that we can build 50 percent of the expected new generation capacity with renewable energy sources in the next 11 years?

Mr. GLAUTHIER. Maybe we need to share some of our detailed projections. The information I have is that 14 percent of the new capacity would have to be renewable. So, it may be that some of our expectation is also co-firing of existing coal fire capacity, for example, with biomass or some other changes that would help to meet the target.

Mr. BARTON. Okay. Well, we expect an expanding market. Perhaps your projectors expect a contracting market, so that might be why you only get at 14 percent. But we will work on that.

I yield back to the gentleman from Tennessee.

Mr. BRYANT. Thank you, Mr. Chairman. I did want to comment on that when I ask a couple of more questions, just in a summary conclusion.

But just a couple of other questions. Does the administration support the bill introduced by Mr. Waxman to amend the Clean Air

Act to require older coal power plants in the Midwest and the Southeast to meet new performance standards?

Mr. GLAUTHIER. We have not taken a position on that legislation yet.

Mr. BRYANT. And do you know when you might?

Mr. GLAUTHIER. No, I don't have any prediction or estimate.

Mr. BRYANT. Okay. Does the—have you taken a position on the Clean Air Act provisions of the Pallone bill, which sets national emission standards for nitrogen oxide particulates, carbon dioxide, and mercury? In June, Secretary Richardson said the administration believed that these clean air amendments should not be included in electricity legislation. Is that still the position?

Mr. GLAUTHIER. Yes, the administration's view is it should not be included in the electricity restructuring legislation but should be dealt with in consideration of the Clean Air Act.

Mr. BRYANT. Well, I appreciate that.

I just tell you from the standpoint of what I am hearing, and again I am focusing on the Southeast, but, you know, I hear other things too. In these—the renewable standards, as our chairman indicated, just don't appear to be realistic, maybe even up here, but certainly from what I am hearing back in my area. It is just not reasonable at this point, that number. While we are all committed to going that direction, we are concerned as this deregulation process unfolds that we not go overboard on this with unattainable standards. We are going to be asking in particular the TVA to compete again in a deregulated world—and Mr. Whitfield is not here—but a good part of the power is generated through coal by our plants, and we are already dealing with clean air standards and trying to go that direction, but I think we are going to need greater transition periods and a little bit more flexibility in those areas.

Mr. GLAUTHIER. We are more optimistic. I understand we are at about 2.3 percent renewables already, so the next 10 years our projection is that we can get to 7.5 percent, although it is a bit ambitious. That is why we have built in a cost cap in our proposal, as well, so that if it is more expensive than the 1.5 cents per kilowatt hour that we have built in, that would take effect, and we would not see people spending higher amounts of money just to meet a target.

Mr. BRYANT. Thank you for your efforts there, and would yield back my time.

Mr. BARTON. Thank the gentleman.

We noticed that we are graced with the presence of the distinguished Congressman from Staten Island, New York, the Republican parties own Vito Fossella who says he has no questions but he has this cryptic note that says, "Go Yankees."

I would point out that the Dallas Stars beat the Buffalo something-or-anothers in hockey, and the San Antonio Spurs beat the something-or-nothing Knickerbockers from New York.

Mr. FOSSELLA. Go Yankees.

Mr. BARTON. Does the gentleman wish to ask any questions?

Mr. FOSSELLA. No.

Mr. BARTON. Okay. Mr. Shimkus says he has one question before we let this gentleman go.

Mr. SHIMKUS. Yes, I want to be the kinder, gentler Shimkus and apologize for getting so excited.

I want to go back to really the same issue, trying to understand if they are the RTOs, whether it be ISOs or whether they are transcos; ISOs being what Illinois has opted for, in fact, made mandatory to ensure against market power. Why is that not enough to—two additional questions—what additional powers are needed and how does cost-based rates help in this discussion?

Mr. GLAUTHIER. It may be that the provisions there for the—in the Illinois statute for transmission will do the job, and what we want is for FERC to have the authority just to be able to oversee that and be sure that it doesn't—that nothing more is needed. There is market power that can exist at the generation level or the link between generation and retial sales, so it is not all in transmission, but it may be the position of the utility in the marketplace that is still restricting competitive choice, competitive options. And, so that aspect of market power also needs to be addressed.

Mr. SHIMKUS. What about cost-based rates? Is that—how do you see that being helpful in the market power debate?

Mr. GLAUTHIER. Well, of course, we all want to move away from cost-based rates and really see——

Mr. SHIMKUS. But it is being promoted by folks as a solution to the market power, at least in the short-term, however you define that.

Mr. GLAUTHIER. It may have a role in a transition period in some cases, but it is certainly something we want to move away from as an overall pattern. So, I would look at that as a potential transition action or step.

Mr. SHIMKUS. Thank you, Mr. Chairman. I yield back.

Mr. BARTON. Since we have let a Republican ask one more question, we are going to let a Democrat ask one more question. Mr. Sawyer. But this will be the last question before we release this witness.

Mr. SAWYER. Thank you, Mr. Chairman.

With a number of questions, we have been talking about how this transmission system can grow and accommodate an uncertain future. Can you comment on siting decisions and the administration's point of view with regard to decisions, particularly in circumstances where a State might not be the direct beneficiary of siting decisions that were nonetheless needed in order to evolve a transmission system?

Mr. GLAUTHIER. We think that siting decisions ought to be addressed somehow in a regional context. We would hope the States would work together to try to deal with those questions. Ultimately, the authority rests with each State on the individual siting decisions, but we want to encourage the planning and cooperation on a regional basis.

Mr. SAWYER. In that sense, do you think it should be different from natural gas pipeline siting decisions?

Mr. GLAUTHIER. Yes.

Mr. SAWYER. Why?

Mr. GLAUTHIER. Really based on the historical patterns that over the decades in which the utility industry has grown up, the States

have had the authority, and so it has never been done really on a regional basis.

Mr. SAWYER. I am really not trying to—do you believe that is compatible with regional markets and the growth and evolution of the grid needed to serve them?

Mr. GLAUTHIER. What we would like to do is encourage regional cooperation and for regions to work together on the questions of new capacity additions, new transmission expansions, and those siting decisions naturally will be a part of that. But we would like to see it done in a way that still respects the States' individual authorities, as well.

Mr. SAWYER. Thank you, Mr. Chairman.

Mr. BARTON. Thank you.

Now, we do want to release this witness.

Mr. MARKEY. Mr. Chairman?

Mr. BARTON. The gentleman from Massachusetts?

Mr. MARKEY. Is it possible that I could ask an extra question, as well?

Mr. BARTON. Yes. I don't want to let the pandora's box too open. We have got two more panels today and a series of votes in the next 4 or 5 minutes, but the gentleman from Massachusetts has certainly been a positive contributor to the dialog. Final exam time is almost here, so if you like—if you could just ask 1 or 2, though.

Mr. MARKEY. Thank you, Mr. Chairman. I appreciate it.

Earlier, the gentleman from North Carolina suggested that I don't trust markets and I just want more Government regulating, because I have higher rates in New England, and therefore want to raise rates again down in North Carolina.

And I would like to respond to that.

Mr. BARTON. Well, let us don't pick a food fight between Massachusetts and North Carolina right now, if possible.

Mr. MARKEY. I don't think that this will be considered a food fight. This will be—you know, my wife always tells me, "You have two choices in life: reenactment or reconciliation."

Mr. BARTON. Okay.

Mr. MARKEY. And reenactment, very bad—reenactment is very bad.

Reenactment leads to escalation. So, this is an attempt at reconciliation, which is good, very good.

Mr. BARTON. Oh, Okay.

Mr. MARKEY. We should always be trying to achieve it.

Mr. BARTON. Well, just notice that I am in the middle here.

Mr. BURR. The gentleman from Massachusetts won't mind if I stay seated for this, will he?

Mr. MARKEY. That is okay.

So, first, I do trust markets, but I don't trust monopolies. And one thing I have discovered over the years is that markets are very inefficient when it comes to eliminating Government-granted monopolies. It just doesn't happen. Government action is sometimes needed to break up a monopoly and create a real market, because——

Mr. BARTON. This is supposed to be a question.

Mr. MARKEY. I understand that, but sometimes I find that the best questions are in the form of answers.

Mr. BARTON. We will put the gentleman on one of the panels if he wishes.

Mr. MARKEY. Well, let me ask you this, Mr. Gauthier: Do you find it curious that all the organizations representing consumers and competitors oppose the Barton bill, while the incumbent monopolists like it? That is more pointed than I wanted to make it, but——

Mr. GLAUTHIER. There are elements we think need to be added to the bill to provide consumer protection.

Mr. MARKEY. But is that an interesting—do you think it is accidental that all the competitors and consumers are on one side, and the monopolists are on the other side?

Mr. GLAUTHIER. It is an interesting observation. We think there needs to be some perfection of the bill before we can support it.

Mr. MARKEY. Okay, good. Well, that will be our goal then, and I thank you, Mr. Chairman, for allowing me to ask that question.

Mr. BARTON. All right. Seeing no other member who wishes to ask one more question, we are going to release this witness.

We want to thank the administration and the Department for your cooperation, and we do look forward to working with you. I told the Secretary this, and I want to tell you this: We really appreciate the staff and their cooperative attitude in working with our staffs.

So, you are released from this subcommittee.

Now, we have a series of votes. We have 3 to 4 votes. That is going to take probably 30 minutes. So, we are going to recess for lunch, because we have to, not because we want to, and we will reconvene at 1:30. And if nobody else is in the room, I want myself, and—which I will be here—and the FERC commissioners, okay?

So, we are recessed until 1:30 Eastern Daylight Savings Time.

[Whereupon, at 12:34 a.m., the subcommittee recessed, to reconvene at 1:31 p.m., the same day.]

Mr. BARTON The subcommittee will come to order.

We actually have all the commissioners here I think. We want—well, we have got one more here.

We want to welcome the distinguished Federal Energy Regulatory Commission to the Subcommittee of Energy and Power. Today, we are going to start off with the Chairman, the distinguished Mr. James Hoecker, then we are going to go from the Chairman's left or the committee's right—to Ms. Bailey, Ms. Breathitt, Mr. Hebert, and Mr. Massey.

We are going to recognize each of—your written statements are in the record in their entirety, and we are going to recognize each of you for such time as you may consume, which I am a little bit leery of doing since some of you are from the South and talk slowly. But we really do want to hear your comments, but I would encourage you to try to limit them to 5 to 10 minutes so that we can have some time to ask questions.

So, Mr. Chairman, you are recognized, and then after you we will go with Ms. Bailey and then right on down the road.

STATEMENTS OF HON. JAMES J. HOECKER, CHAIRMAN, ACCOMPANIED BY HON. VICKY A. BAILEY, COMMISSIONER; HON. LINDA KEY BREATHITT, COMMISSIONER; HON. CURT L. HEBERT, JR., COMMISSIONER; AND HON. WILLIAM L. MASSEY, COMMISSIONER, FEDERAL ENERGY REGULATORY COMMISSION

Mr. HOECKER. Thank you, Mr. Chairman. Chairman Barton, members of the subcommittee, it is again a privilege for me to appear before you; this time, in general support of H.R. 2944.

Mr. Chairman, I recognize the difficulty of sorting through the complex facets of electric restructuring to find the appropriate combination of forward-looking initiatives that will serve the American energy consumer well, doing neither too much nor too little, employing Federal authority effectively but not excessively. We share with you a faith in the benefits of competition and in the ability of public policy to ensure that there is an efficient and equitable market structure within which competition can flourish. I, therefore, applaud your desire to enact legislation, and I pledge to help you do so.

I agree with the Deputy Secretary that electricity markets require certainty now more than ever, that demands on the system require a boost in generation reserve margins and transmission capacity, and that the Congress should now speak to how it would have this industry evolve in the future.

In response to the Energy Policy Act of 1992 and our own Order 888, competition is growing in electric generation and marketing sectors. New challenges to system reliability are more in evidence. The time has therefore arrived to strengthen the platform upon which competition and reliability must stand. And by that I mean non-discriminatory access to the integrated network of high voltage transmission.

For 2 years, I have testified before both Houses of Congress that the newly competitive bulk power market needs legislative assistance to do four things: To place all electric transmission under the Commission's jurisdiction for purposes of ensuring non-discriminatory access to transmission services; second, to clarify and reinforce the Commission's authority to promote regional transmission organizations; third, to protect the integrity of transmission service through mandatory reliability rules established by self-regulating organizations subject to FERC oversight, and, fourth, to reform the Public Utility Holding Company Act.

Now, although I recognize that the administration and this committee have a much broader restructuring agenda than does our Commission, I am pleased to say that H.R. 2944 takes these four key issues I have mentioned head on, and with some reservations, I would say it does a good job.

In my written testimony, I make several suggestions for your further evaluation, but let me highlight a few before I close. First, State regulators, appearing on the next panel as the National Association of Regulatory Utility Commissioners, would give utilities a chance to avail themselves of the opportunity to join an RTO voluntarily but would then allow the FERC to require a utility to join an RTO if that utility had not done so voluntarily.

Now, that is my position, as well. Our proposed rule already sets forth a timetable for voluntary utility actions in this connection. However, I view the statute mandate that you propose as a very sound alternative.

Second, three of my colleagues and I asked the Congress to help us ensure that all uses of the transmission system are treated comparably in the face of a troublesome recent decision in the 8th Circuit Court of Appeals. An addition to the bill is suggested in my testimony to address this problem.

And, third, I note that other pending legislation would enhance the Commission's authority to address market power outside the context of mergers, and I support such measures. As the Commission moves toward light-handed regulation, its ability to monitor the market and to identify and address exercises of residual market power becomes ever more important.

In conclusion, my objective is to help create a market structure that ultimately will allow markets, and not regulators, to determine the price of wholesale electric power. You will notice, I am sure, that the members of the Commission do not entirely agree on how to get to competitive electricity markets. We do agree that competition is the goal, however. We do agree that RTOs have substantial benefits, that reliability must be protected, and that market power must be constrained in the context of mergers and elsewhere.

The question for the subcommittee, and in fact for our Commission as well, is how proactive and supportive we should be in pursuit of these objectives.

Mr. Chairman, I thank you for the opportunity to offer my views here this afternoon, and I look forward to your questions.

[The prepared statement of Hon. James J. Hoecker follows:]

PREPARED STATEMENT OF HON. JAMES J. HOECKER, CHAIRMAN, FEDERAL ENERGY REGULATORY COMMISSION

Mr. Chairman and Members of the Subcommittee: Good morning. My name is James J. Hoecker, Chairman of the Federal Energy Regulatory Commission. Thank you for the opportunity to appear before you today. My testimony will address the need for Federal electricity legislation generally and the provisions of H.R. 2944 in particular.

In prior testimony before this and other subcommittees of the House of Representatives, I have recommended that Congress enact legislation to address several matters that are critical to achieving fully competitive, reliable wholesale electric power markets. These include placing all electric transmission in the continental United States under the same rules for non-discriminatory open access and comparable service; reinforcing the Commission's authority to foster regional transmission organizations; establishing mandatory reliability rules to protect the integrity of transmission service, relying on a self-regulating organization with appropriate Federal oversight of rule development and enforcement; providing the Commission with appropriate authority to remedy market power; and, reforming the Public Utility Holding Company Act (PUHCA).

As discussed below, the provisions of H.R. 2944 advance a number of these policy goals. I commend you, Chairman Barton, for developing this bill. I will suggest some additions and modifications for your consideration.

I. INTRODUCTION

Traditional regulation of electricity sales for resale in interstate commerce—*i.e.*, the wholesale or "bulk" power market—has been based on the recognition that electric utilities were operating as natural monopolies. Consequently, during most of this century, federal agencies addressed market power and ratepayer interests, not by promoting competition, but by strict oversight of the terms of services and cost-

of-service rates. In the 1980s and early 1990s, however, several developments in the electricity generation sector indicated that the interests of utility ratepayers could be better protected by competition in wholesale power markets than by cost-based regulation. The benefits of replacing traditional regulation with competition became evident in other industries, such as trucking, railroads, long-distance telecommunications and natural gas. In the Energy Policy Act of 1992, Congress took important steps toward competition in wholesale power markets, by providing the Commission with greater authority to order transmission owners to transmit power for other buyers and sellers in the wholesale market, and by modifying PUHCA to eliminate a key barrier for new generators entering these markets. Electric generation units built and operated independently of traditional utilities had already proved to be competitive and reliable parts of the electric system.

Consistent with these changes in the industry, the Commission in 1996, through a major rulemaking called Order No. 888, ordered open, non-discriminatory access to the transmission facilities of public utilities for wholesale market participants. This open access obligation prohibits public utilities from discriminating against competitors' transactions in favor of their own wholesale sales of power. Order No. 888 has enhanced competition in wholesale power markets significantly, although it has not opened the grid to competition entirely.

Today, the promotion of competition and reliable service among power suppliers in wholesale markets remains the Commission's primary goal in this area. The Commission's fundamental regulatory objectives are: (1) to substitute competition for price regulation in wholesale power markets to the extent possible; and (2) to ensure that transmission service is made available under non-discriminatory terms and conditions so as to enable competition among suppliers of electricity in these markets. Transmission facilities form an integrated, interstate grid that is essential for delivering power, in the same way the interstate highway system allows trucks to deliver other commodities across state boundaries pursuant to private contracts. The transmission grid, however, is owned by individual utilities and, absent regulation, these utilities can effectively prevent the use of these facilities by their competitors. Thus, regulation of transmission is necessary to ensure open access, non-discrimination and reasonable rates. Effective regulation of the relatively small transmission portion of the utility business (it accounts for about only three to four percent of the average price of energy delivered to the home) enables competition in the much larger generation sector to produce sizeable ratepayer benefits.

The Commission is seeking to use its current authority to promote competitive wholesale markets. The Commission has also made a determined effort to assist states choosing to pursue retail market competition, which ultimately will succeed only if there is a competitive wholesale market. However, most of the federal regulatory framework dates from before competition became significant in this industry and, in some key respects, now impedes these efforts. I therefore support Federal legislative reforms that will better enable the Commission to promote competition and reliability in wholesale markets as well as facilitate retail competition initiatives, as appropriate.

II. TRANSMISSION ISSUES

A. Open Access

Fair and open access to reliable transmission service is an essential predicate to competition in bulk power markets. Congress expressly recognized this fact in the Energy Policy Act of 1992, by giving the Commission limited new authority under Federal Power Act (FPA) section 211 to require utilities to provide transmission service to others on a case-by-case basis. The Commission later, in Order No. 888, relied primarily on its traditional authority to prevent undue discrimination when it ordered public utilities to provide generic open access to their transmission facilities. The Commission concluded that Order No. 888 was necessary to support competition in wholesale power markets.

I view **Section 102(a)(1)** of H.R. 2944 as a confirmation that the open access provisions of Order No. 888 are completely consistent with Congressional goals. H.R. 2944 would clarify the Commission's authority to require open access transmission services under FPA sections 205 and 206, and would apply this clarification to any "rule or order promulgated by the Commission before, on, or after" the bill's enactment. I support this provision as eliminating any remaining uncertainty about the Commission's authority to adopt the Order No. 888 open access transmission requirements.

H.R. 2944 would extend the Commission's open access authority to all "transmitting utilities," as defined by the FPA. Under current law, the open access obligations of Order No. 888 apply only to transmission facilities owned or operated by "public

utilities,'' as defined by the FPA. In other words, approximately one-third of the transmission grid in the contiguous 48 States is not subject to the Commission's open access requirements, even though these facilities are generally integrated with, and are integral to the operation of, the rest of the network. This portion of the grid is owned primarily by federally-owned utilities, electric cooperatives that are financed by the Rural Utilities Service, and some municipal utilities. While some of these entities have chosen to offer open access transmission service voluntarily, many others do not. These gaps in open access to the transmission grid inevitably impede the development of fully competitive wholesale power markets. Only federal legislation making all utilities subject to the same open access requirements can remedy this problem.

I believe that all transmitting utilities should be subject to the same transmission rules. Open access to a seamless transmission grid by all electricity suppliers is essential if the Congress and the Commission intend to guarantee that buyers and sellers of electricity have as many choices as possible. I note, however, that H.R. 2944 narrows the definition of transmitting utilities to exclude certain utilities that transact within the Electric Reliability Council of Texas (ERCOT). While the Commission does not have authority to regulate transmission within ERCOT as it does elsewhere, it has had authority since 1978 to order transmitting utilities, including those that transmit within ERCOT, to provide transmission services in some circumstances under FPA section 211. Although used sparingly, this authority has been used to promote competitive access. Central Power & Light Co., *et al*., 17 FERC ¶61,078 (1981); City of College Station, Texas, 86 FERC ¶61,165 (1999); Tex-La Electric Cooperative of Texas, Inc., 69 FERC ¶61,269 (1994). The proposed change in definition would exempt those utilities that transact only within ERCOT from the current, limited section 211 authority as well as the broader open access authority addressed in H.R. 2944 itself. The Congress should leave the Commission with section 211 authority in this area.

B. Regional Transmission Organizations

In Order No. 888, the Commission encouraged, but did not require, the formation of independent system operators (ISOs). The Commission found that ISOs would promote broader, regional power markets and provide greater assurance of non-discrimination. Since 1996, six ISOs have been established (in California, the mid-Atlantic states, New England, New York, the Midwest, and Texas). Four of these are currently operational.

The Commission is now seeking to address the remaining impediments to full competition, which fall largely into two categories. First are the engineering and economic inefficiencies inherent in the current operation and expansion of the transmission grid. For example, each separate transmission operator makes independent decisions about the use, limitations, and expansion of its part of the grid, but the interconnection of the separate transmission systems causes each such action to immediately affect other parts of the grid. With the increase in competition, the grid is being stressed by many new entrants and by new transactions using two or more systems in a region, presenting challenges to the historical approach to maintaining the reliability of separate, but interconnected, systems. Also, competitive markets must evolve into regional markets if they are to thrive, and the efficiency gains of competitive markets will be imperiled unless regional solutions are used for pricing transmission services and managing regional constraints and expansion needs.

The second category of impediments are the continuing opportunities for transmission owners to unduly discriminate in the operation of their transmission systems so as to favor their own or their affiliates' power marketing activities. In the wake of Order No. 888, many market participants continue to allege, and the Commission has in some cases confirmed, that transmission service problems related to discriminatory conduct remain.

To address these impediments, the Commission has proposed new rules to promote the voluntary formation of regional transmission organizations (RTOs) such as ISOs and independent companies that own and operate only transmission facilities (transcos). Such institutions are encouraged to form in the near future, under a schedule specified in the proposal. Notice of Proposed Rulemaking on Regional Transmission Organizations, 64 Fed. Reg. 31,389, FERC Stats. & Regs., ¶32,541 (1999).

An RTO is an organization formed to administer the operation of the transmission system on behalf of all the participants in the market. It may be a for-profit or non-profit institution but it must be independent of all other financial interests of power market participants. It should cover an appropriately configured region and have adequate operational control over the transmission grid. If properly designed, an RTO can ensure the non-discriminatory operation of the transmission grid, elimi-

nate pancaked transmission charges for using transmission systems owned by different utilities, reduce and better manage congestion on the transmission lines, and facilitate transmission planning on a multi-state basis.

Section 103 of H.R. 2944 would require each transmitting utility to establish or join an RTO by January 1, 2003, and to file an application for its proposed action with the Commission by January 1, 2002. I fully support the bill's goal of having utilities participate in an RTO.

However, I offer the following suggestions for improving H.R. 2944's provisions on RTOs. First, I would advance the deadline for participation in RTOs by at least one year, so that consumers can begin receiving the substantial benefits of RTOs much sooner. Because transmission systems are already regionally integrated, economic efficiency gains from the coordinated operation of transmission over a broad geographic area are readily attainable. It is therefore increasingly difficult to justify delaying such benefits to the public. The Commission's RTO proposal calls for RTOs to be operational by December 15, 2001.

Second, let me address proposed FPA section 202(h)(2), which addresses the standards RTOs must meet. Although the topics of the four standards proposed for FPA section 202(h)(2)—independence, geographic scope and configuration, operational authority and expansion—are generally consistent with key considerations identified in the Commission's proposed rule, I believe the bill should not attempt to codify detailed prescriptions for each of the four policy standards. The Commission has yet to evaluate all of the comments submitted on its proposed rules. As importantly, competitive markets will continue to evolve in ways that are difficult to predict. Detailed standards that appear appropriate today may be inappropriate in future years. For example, the bill "deems" the requirement for independence to be met when market participants own passive, nonvoting interests or 10 percent or less of the voting interests. It is not appropriate to lock the details of these standards into statutory text, given the possible need to adapt the standards to future changes in the industry before the FPA is again modified. I recommend a somewhat different approach; namely, that the Congress should preserve the Commission's discretion to adapt policy to changing circumstances, especially with respect to administering the key policies of independence and regional scope and configuration. The Commission as well as the institutions we regulate need the ability to adapt to changing market conditions and to changing regional needs.

Third, under Section 103 of H.R. 2944, the Commission must approve an application to join or establish an RTO if the RTO meets the prescribed standards. It specifically prohibits the Commission from requiring a utility to participate in a different RTO. Although I believe the Commission must and will apply standards fairly and promptly, the language in the bill could be construed as allowing the Commission only to approve or disapprove an application, but not to modify it. To ensure that RTOs yield their expected benefits as soon as possible, and consistent with the Commission's authority under other FPA sections, such as sections 203, 205 and 206, the Commission should have the procedural flexibility to work with the applicants to modify a flawed proposal, instead of simply disapproving a deficient or noncomplying application and thereby imposing the burden of reapplication. Further, the concept of RTOs, while sound, is a work in progress and the Commission should be able to approve such applications subject to conditions when necessary to make them consistent with the public interest.

Finally, Section 103 of H.R. 2944 states that "[t]he Commission shall encourage incentive transmission pricing policies" for RTOs. Section 103 states that such pricing policies include incentives for transmitting utilities to form RTOs, as well as incentives for RTOs to eliminate rate pancaking, to minimize cost shifting and to encourage adequate investment in and expansion of the transmission grid. I support these goals. The Commission has already solicited comment on whether and how to employ such incentives in the context of the ongoing RTO rulemaking.

C. Reliability

The changes in the industry in recent years have created a need for new tools for ensuring the reliability of the transmission grid. In the past, reliability was addressed through the voluntary cooperation of transmission owners. Today, industry participants increasingly recognize that cooperative efforts among transmission-owning utilities may not be sufficient in a competitive environment, and that a mandatory system for ensuring the reliability of the grid is needed. This recognition has caused the industry to begin seeking the Commission's involvement on reliability issues, even though the Commission has not regulated system reliability historically and it has no express authority to do so. For example, while the Commission has authority to address discrimination in jurisdictional transmission services, it has no explicit statutory role in setting or reviewing particular reliability standards or in

ensuring the security of the electrical system or the adequacy of supply. That was left largely to the industry and the States.

As I have testified previously, Congress should make compliance with appropriate reliability standards mandatory. There appears to be an industry consensus that it can continue to work collaboratively to develop reliability standards, using a process in which all market sectors are fairly represented. I believe that, if the standard-setting process is representative of all stakeholders, a high degree of self-regulation is appropriate. However, sufficient Federal oversight will be needed to ensure that the standards set by that process are adequate, not unduly discriminatory or anti-competitive, and enforceable, and to ensure that enforcement of the standards is effective and fair.

Section 201 of H.R. 2944 meets these reliability concerns. Section 201 also recognizes the role of the States in ensuring the reliability of local distribution facilities by preserving existing State authority over local distribution facilities unless the exercise of such authority would unreasonably impair the reliability of the bulk power system. I believe that any Federal legislation should also preserve for the States any reliability practices that they have historically engaged in with respect to bundled transmission in their jurisdictions, *provided* that such practices are consistent with the applicable regional or national standards and such reliability practices do not unduly impair competition in bulk power markets.

D. Undue Discrimination and Comparability

In Order No. 888, the Commission required public utilities to offer transmission service to third parties under the same rates, terms and conditions as the utilities applied to themselves for their own wholesale and retail sales of generation. Further, load-serving utilities thereafter were to take transmission service for their wholesale sales of generation under the same tariff as everyone else. In other words, the Commission required "comparability" of transmission services for a public utility and its transmission customers. Comparability is critical to ensuring that competition in power markets is not distorted by preferential or discriminatory transmission services.

A recent court decision may have placed a cloud on the Commission's ability to ensure comparability and support competition. The appellate court decision in *Northern States Power Co., et al., v. FERC,* No. 98-3000 (8th Cir., May 14, 1999, *rehearing denied,* September 1, 1999), if interpreted and applied broadly, may prevent the Commission from enforcing rules that provide for comparable terms and conditions of service for all users of transmission, including pro rata curtailments of transmission service used by a utility for in-state "native load." Arguably, this court decision may allow one state to require its utilities to establish a preference for in-state uses of the transmission grid to the detriment of consumers in other states whose utilities depend on comparable access to electricity supplies over the same transmission facilities. If states can effectively establish preferential transmission services for the utilities they regulate, the wholesale power markets will become balkanized and competition in those markets could wither.

I suggest revising Section 101 of H.R. 2944 to address this concern. In particular, I suggest adding a provision at the end of FPA section 201(a), as modified by section 101(b)(1) of the bill, stating that:

> In regulating the transmission of electric energy under any provision of this Part [Part II of the FPA], the Commission shall have exclusive authority to establish rates, terms and conditions of transmission service that are just, reasonable and not unduly discriminatory or preferential, including rates, terms and conditions that prevent or eliminate undue discrimination or preference associated with a public utility's or transmitting utility's own uses of its transmission system to serve its wholesale and retail electric energy customers.

Such a provision would clarify the Commission's authority to ensure that transmission services within its exclusive jurisdiction are provided on a basis that is comparable to, *i.e.*, no less favorable than, other transmission services provided by a transmitting utility, and that competition among power suppliers is not distorted.

E. Expansion of the Transmission Grid

Section 105 of H.R. 2944 would allow the Commission, upon application, to order a transmitting utility to enlarge, extend or improve its transmission facilities. Before doing so, the Commission would be required to refer the matter to a joint board for recommendations on the need for, design of, and location of the proposed expansion. The provision retains the states' traditional siting authority.

I do not see a current compelling need for the Commission to be given the authority specified in section 105 of H.R. 2944. Instead, my expectation is that RTOs will help address many issues concerning expansion of the transmission grid including

the need for new facilities and who pays for them. However, even if an RTO were to recommend system expansion, nothing could be done without the cooperation or acquiescence of state siting authorities. Nothing in H.R. 2944 proposes to alter that.

III. MERGER REVIEW AND MARKET POWER

Under FPA section 203, the Commission must review proposed mergers, acquisitions, and dispositions of jurisdictional facilities by public utilities, and must approve such transactions if they are consistent with the public interest. In evaluating the public interest, the Commission considers a transaction's effects on competition, rates, and regulation.

The Commission's jurisdiction over mergers is currently limited in certain ways. First, the Commission has no direct jurisdiction over transfers of generation facilities. It can review transactions involving a public utility only when they involve other facilities that are jurisdictional (such as transmission facilities or contracts for wholesale sales). Second, the Commission lacks direct jurisdiction over mergers of public utility holding companies that have electric utility subsidiaries. While the Commission has construed such mergers to involve jurisdictional indirect mergers of public utility subsidiaries of the holding companies, or changes in control over the jurisdictional facilities of the public utility subsidiaries, the FPA is not explicit on this point. Section 401 of H.R. 2944 would address both circumstances appropriately, clarifying that the Commission has jurisdiction over transactions involving only generation facilities and mergers of holding companies. I support these amendments.

Section 401 of H.R. 2944 also would require the Commission to act on mergers within five months or, for good cause shown, an additional three months. Since the Commission issued its Merger Policy Statement in December 1996, the Commission has taken final action on nearly all mergers within five months after receipt of a complete application. Those actions included review of complex electric and gas-electric mergers, some of them quite large and unprecedented. Therefore, I would expect the proposed deadlines to be adequate, with one caveat. Occasionally a merger raises numerous and genuine issues of material fact that necessitate extensive fact-finding in a hearing context. For example, out of the 30 merger applications filed since issuance of the Commission's Merger Policy Statement, the Commission has acted on 23 of them (the other seven having been filed only recently) and needed to establish an evidentiary hearing with respect to only three of them because there were material facts in dispute. In such cases, the Commission needs more time to resolve such factual disputes than H.R. 2944 would allow. In those infrequent instances when material facts are disputed, an artificially short deadline would leave the Commission with little recourse other than to reject the application.

I note that other pending legislation would enhance the Commission's authority to address market power outside the context of mergers. For example, the Administration's proposed bill, H.R. 1828, would allow the Commission to address market power in retail markets, if asked to do so by a state lacking adequate authority to address the problem. It would also give the Commission explicit authority to address market power in wholesale markets by requiring a public utility to file and implement a market power mitigation plan. H.R. 2050, sponsored by Congressmen Largent and Markey, also contains provisions that would allow mitigation of market power, to the benefit of competition and consumers. Such provisions are particularly desirable in the circumstances where a State lacks adequate authority to address market power issues and seeks FERC's assistance. As the Commission moves toward light-handed regulation, its ability to monitor the market and to identify and address exercises of residual market power becomes more important.

IV. PUHCA

Adopted over 60 years ago to restrain the growth and power of large utility holding companies, PUHCA requires some utilities to comply with restrictions that are not entirely compatible with today's bulk power competition. In some instances, PUHCA encourages the very concentrations of generation ownership and control that undermine competitive power markets. It discourages asset combinations that could be pro-competitive. Thus, PUHCA should be reformed, with one major caveat. Reform legislation should ensure that both the Commission and States have adequate access to the books and records of utilities and their affiliates, to protect against affiliate abuse and ensure that captive consumers do not cross-subsidize entrepreneurial ventures. **Sections 511-524** of H.R. 2944 would satisfy these concerns.

V. CONCLUSION

Competition is growing in the electric generation and marketing sectors, in response to the Energy Policy Act of 1992 and the Commission's efforts to remove barriers to competition. My objective in seeking legislation is to create a market structure that ultimately will allow markets—not regulators—to determine the price of wholesale electric power. Effective regulation of transmission facilities that are essential for delivering power is critical to ensuring that consumers continue to receive increasing benefits from competition in power markets. Likewise, effective restraints on the exercise of market power in these newly competitive electricity markets is essential to advancing competition.

Thank you again for the opportunity to offer my views here this morning. I would be pleased to answer any questions you may have.

Mr. BARTON. Thank you, Chairman.

We would now like to hear from Commissioner Bailey.

STATEMENT OF HON. VICKY A. BAILEY

Ms. BAILEY. Good morning, Mr. Chairman and members of the subcommittee. I thank you for inviting me, along with all of my colleagues, to testify this morning on H.R. 2944, the Electricity Competition and Reliability Act of 1999.

Having joined the Commission 6½ years ago, the electric utility industry the Commission regulates today bears little resemblance to the industry I first encountered as a Federal regulator in 1993.

Competition in the marketplace is now clearly the driving force. Electric utilities can no longer afford to be stodgy, conservative enterprises of earlier years. Management is increasingly entrepreneurial in spirit and action. Shareholders as well as ratepayers increasingly are demanding decisive action to promote transaction-related revenues and to cut costs.

I have been reluctant to call for sweeping Federal energy restructuring legislation, and I have been reluctant to champion prescriptive, industry-wide action by the Commission. My concern is that any such overreaching action will stifle the type of industry innovation and flexibility that has marked the last few years. I am extremely hesitant to support any major piece of legislation or rulemaking that would lock into place a 1999-vintage vision for the industry when that vision might very well be overtaken by technological as well as other advances in future years.

Competition requires that industry participants enjoy the opportunity to take chances and possibly to make mistakes. But while I encourage risk-taking, and generally favor fewer layers of regulatory review rather than more, I remain mindful of the vital role that utility services provide in the everyday lives of the people of this Nation. America's consumers and industries must remain confident that electric service will remain as reliable as ever. And all of the pro-competitive rhetoric of enlightened commentators and Government officials will amount to nothing if the benefits of competition, through lower prices or increased product offerings, ultimately do not work their way down to all consumers.

In my judgment, H.R. 2944, taken as a whole, does a very good job of threading the needle, allowing utilities to develop their own competitive business strategies, while ensuring that competitive miscalculations do not impair the reliable operation of the grid or limit the availability of low-cost energy services. I commend the subcommittee for its thoughtful and comprehensive review of the issues confronting the many participants in the marketplace, and

its crafting of compromise legislation that represents a careful balance of various concerns and positions.

Let me comment briefly on four of the specific elements of the bill.

One, mergers. The recent trend of consolidation in the increasingly competitive electric utility industry will not abate and probably will accelerate. I also expect new and different kinds of merger proposals, involving different kinds of business combinations, to be presented to the Commission.

I am concerned about the pace of Commission review of the merger applications filed with us. I believe it is inconsistent for the Commission to promote competition on the one hand, while on the other hand failing to respond in a timely and more predictable manner to the efforts of regulated utilities to restructure themselves in a manner that, in their judgment, is best able to respond and adapt to competitive realities. I hope that the possibility of delay or uncertainty in the review of merger applications does not act to inhibit corporate initiatives and innovation.

I sense this same concern in the language of section 401 of H.R. 2944 that limits the time for Commission review to, at most, 240 days from the date of filing. At present, the Commission already is acting on the vast majority of merger applications within that timeframe. Nevertheless, a legislatively mandated 240-day time cap for Commission decision could affect the Commission's processing of harder cases involving the proposed combination of larger utilities.

It effectively eliminates all but the most abbreviated of evidentiary hearings in merger cases. Many commentators undoubtedly will criticize the loss of procedural options currently available to the Commission; I, however, will not. Contested issues of policy and fact can, in almost all merger circumstances, be decided on the basis of the written pleadings filed for the Commission's consideration. And while I am not attached to any single duration of any limitation, I do not find it unreasonable to expect the Commission to act in a timeframe consistent with Congress' view as to the need for timely and predictable action.

As to the rest of section 401, which expands the Commission's merger authority in certain respects, I add my skepticism as to the need for Commission authority to consider the effect of any proposed merger on retail markets. In recent years, State commissions have refrained from asking the Commission to intercede in this area, and have demonstrated that they are quite competent to address the retail implications of proposed utility mergers. I see no reason to add an additional layer of regulatory review.

On the issue of regional transmission organizations, I appreciate section 103 of H.R. 2944, in its reference to encouraging utility innovation and individual design in the formation of RTOs. But I am deeply concerned by a mandate that compels filing by all utilities by January 1, 2002 and RTO participation by January 1, 2003.

I believe that the Commission already possesses sufficient authority under existing law to encourage transmission-owning utilities to cooperate voluntarily with their neighbors to advance regional solutions to lingering competitive and operational problems in wholesale power markets. I would much prefer to allow utilities

to continue the rapid pace of utility restructuring and to work out among themselves and with their customers, with encouragement from the Commission or Congress rather than a legal directive, how best to design regional markets that serve all interests in an efficient and competitive manner.

The vast majority of transmission-owning utilities already are members of regional transmission institutions—i.e. in California, New England, New York, the Mid-Atlantic, the Midwest and most of Texas—or are actively engaged in discussions to form some such type of institution. I support congressional and Commission action that works to encourage this type of regional cooperation, especially with transmission-owning utilities that currently are not public utilities subject to the Commission's regulation and oversight.

I suspect that transmission-owning utilities increasingly will find it difficult, from many different perspectives to refrain from such cooperation. But I do not support congressional or Commission action that, whether phrased subtlety or more overtly, makes the decision for utilities to turn over operational control of the transmission facilities they own to someone else.

For all of these reasons, I believe that a mandate to join a RTO by a date certain is unnecessary and ill-advised. In my judgment, the other provisions of section 103 give transmission-owning utilities all of the incentive they need to participate in an RTO of their choosing.

On the issue of reliability, competition cannot be at the expense of reliability. I have been very impressed with the efforts of the North American Electric Reliability Council and the regional councils that NERC administers to ensure the continued integrity and reliability of the electrical grid. The electric utility industry and the customers it serves are in a much better position to assess and ensure the continued reliability of electric service.

I have refrained from calling out for additional regulatory authority over reliability. Nevertheless, as wholesale power markets become increasingly competitive, and strains are imposed on the continuing reliability of the electrical grid planned and designed for a less competitive, more vertically integrated environment, close cooperation with reliability organizations and State and local authorities become imperative.

For this reason, I have no objection to the language found in section 201 that would clarify the Commission's oversight role by directing it to approve the formation and governance of a self-regulating electric reliability organization. Nor do I object to the Commission's review of mandatory reliability standards and its appellate-type review of implementation and enforcement disputes.

My only hesitation with respect to the reliability provisions of H.R. 2944 would be the Commission's ability to entertain a much larger share of reliability-based issues and disputes, which might have to be decided in close to real-time. My hope is that the need for Commission intervention will be lessened by increasing respect for and adherence to mandatory reliability rules and additional incentives to invest in and expand badly needed transmission capacity.

Finally, I am pleased to see legislative language in section 101 of H.R. 2944 that clarifies the boundaries between Federal and

State jurisdiction over different aspects of electricity supply and delivery. The clarifying language, for the most part, adopts the jurisdictional dividing lines adopted by the Commission in its Order Number 888 rulemaking. Those lines, for the most part, have been accepted by industry participants and State regulatory commissions. This is important in order to eliminate the jurisdictional turf battles and protracted court disputes over ambiguous congressional delegations, in order to ensure that the benefits of increased competition flow through to consumers as quickly and comprehensively as possible.

With that, thank you for the opportunity to present my views on this important piece of Federal legislation, and I would be happy to answer any questions you may have.

[The prepared statement of Vicky A. Bailey follows:]

PREPARED STATEMENT OF VICKY A. BAILEY, COMMISSIONER, FEDERAL ENERGY REGULATORY COMMISSION

Introduction

Good morning Mr. Chairman and Members of the Subcommittee. I thank you for inviting me along with all of my fellow Commissioners to testify this morning on H.R. 2944, the Electricity Competition and Reliability Act of 1999.

I joined the Commission six and one-half years ago. The electric utility industry the Commission regulates in 1999 bears little resemblance to the industry I first encountered as a federal regulator in 1993.

Competition is now clearly the driving force leading the utility industry to restructure. Electric utilities are no longer the stodgy, conservative enterprises of earlier years, favored primarily by widows and orphans. Open access transmission and negotiated, market-based rates are in. Preferential and discriminatory access, and years'-long hearings to assess cost structures and cost allocations, are on their way out. Utility executives are increasingly entrepreneurial in spirit and action; shareholders and ratepayers increasingly are demanding decisive action to promote transaction-related revenues and to cut costs.

Utilities have responded to the advent of competition in a number of different ways. One business strategy is to concentrate on core, niche services. A number of utilities have reached the conclusion that they can best respond to competitive forces by concentrating on their "wires" business; i.e., focusing on electrical transmission and distribution. These utilities have decided to sell off their generating assets—sometimes at a price far in excess of book value, with the proceeds often going to reduce or eliminate their exposure to uneconomic or "stranded" generation investment. Other utilities have decided to focus their efforts on power generation and marketing.

Another business strategy is to remain vertically integrated and to offer an array of different utility products and services. Some utilities have reached the conclusion that they can best flourish in a competitive environment by getting larger and developing economies of scale. For this reason, the Commission has received numerous applications in recent years from utilities proposing classic "horizontal" combinations at the same level of the market (generation, transmission). Other merger applications reflect a recent trend toward "convergence" or "vertical" combinations between electric and natural gas utilities. I expect these trends to continue—indeed, accelerate—and I would not be surprised to see future convergences between electric utilities and other types of industries, such as telecommunications and Internet providers.

Finally, electric utilities are increasingly finding that it is in their best interest to cooperate voluntarily with their neighbors to develop regional institutions that promote reliable operation of, and non-discriminatory access to, the grid.

Who can best claim credit for these dramatic developments? To some extent, we regulators and legislators can. Congress can be quite proud of its legislative accomplishments, such as the Public Utility Regulatory Policies Act of 1978, that (despite unfortunate side-effects) introduced competition into the wholesale power supply market by encouraging the entry of non-traditional, independent power producers. Moreover, the Energy Policy Act of 1992 greatly accelerated the development of competitive markets by offering power suppliers additional ways to reach willing buyers. This Commission can be proud of its efforts in recent years—such as the promotion

of non-discriminatory, open access transmission service—to ensure that the benefits of increased competition are not confined to only a few of the largest industry participants.

But, in my judgment, industry participants themselves deserve most of the credit for the restructuring of the industry and the competitive evolution of the market. Despite a reputation for conservatism, electric utilities have not been hesitant to adopt bold new strategies to take advantage of the opportunities that competition has to offer. Frankly, I have seen little industry resistance to the pro-competitive, open access policies initiated by federal and state legislators and regulators. To the contrary, I have been impressed by the degree of sophistication and innovation adopted by different utilities in different regions of the country to respond in different ways to competitive pressures and opportunities.

For this reason, I have been reluctant to call for sweeping federal energy restructuring legislation. And I have been reluctant to champion prescriptive, industry-wide action by the Commission. My concern is that any such overreaching action will stifle the type of industry innovation and flexibility that has marked the last few years. New ideas and concepts for utility governance and operation are being brought to my attention every week. Some of them will flourish, and others will undoubtedly prove unacceptable. I have no grand design for the utility industry of the next millennium. I am extremely hesitant to support any major piece of legislation or rulemaking that would lock into place a 1999-vintage vision for the industry, when that vision might very well be overtaken by technological or other advances in future years.

Competition requires that industry participants enjoy the opportunity to take chances and, possibly, to make mistakes. But while I encourage risk-taking, and generally favor fewer layers of regulatory review rather than more, I remain mindful of the vital role that utility services provide in the everyday lives of the people of this nation. America's consumers and industries must remain confident that electric service will remain as reliable as ever. And all of the pro-competitive rhetoric of enlightened commentators and governmental officials will amount to nothing if the benefits of competition—through lower prices or increased product offerings—ultimately do not work their way down to *all* consumers.

In my judgment, H.R. 2944, taken as whole, does a very good job of threading the needle—allowing utilities to develop their own competitive business strategies, while ensuring that competitive miscalculations do not impair the reliable operation of the grid or limit the availability of low-cost energy service. I commend the Subcommittee for its thoughtful and comprehensive review of the issues confronting the many participants in the marketplace, and its crafting of compromise legislation that represents a careful balance of various concerns and positions.

I continue to comment briefly on a few of the specific elements of the bill.

Mergers

I have already explained my belief that the pace of merger activity in the electric utility industry will not abate and, probably, will accelerate. I also expect new and different kinds of merger proposals, involving different kinds of business combinations, to be presented to the Commission.

I have expressed my concern on numerous occasions as to the pace of Commission review of the merger applications filed with us. I believe it would be inconsistent for the Commission to promote competition on the one hand, while on the other hand failing to respond in a timely and more predictable manner to the efforts of regulated utilities to restructure themselves in a manner that, in their judgment, is best able to respond and adapt to competitive realities. I hope that the possibility of delay or uncertainty in the review of merger applications does not act to inhibit corporate initiative and innovation.

I sense this same concern in the language of section 401 of H.R. 2944 that limits the time for Commission review to, at most, 240 days from the date of filing. At present, the Commission already is acting on the vast majority of merger applications within that time frame. Legislative language imposing a time cap will not affect in any significant manner the Commission's processing of the "easy" merger cases it receives for review.

It will, however, affect the Commission's review of harder cases. I suspect that the industry is increasingly exhausting the limited scope of potential mergers that present little concern for their effect on competition, rates and regulation, and will increasingly present to us mergers of larger utilities that will attract a significantly higher degree of opposition and analytical scrutiny. The Commission already has set two such merger applications—involving American Electric Power and Central and South West in one case, and Western Resources and Kansas City Power & Light in another—for hearing; those cases are awaiting decision by the administrative law

judges and, ultimately, by the full Commission. The Commission will face similar pressure to set other large mergers—such as those recently proposed by Northern States and New Century in one recent announcement, and PECO and Commonwealth Edison in another—for lengthy, trial-type hearings.

A legislatively-mandated 240-day time cap for Commission decision effectively eliminates all but the most abbreviated of evidentiary hearings in merger cases. Many commentators undoubtedly will criticize the loss of procedural options currently available to the Commission; I, however, will not. Contested issues of policy and fact can, in almost all merger circumstances, be decided on the basis of the written pleadings filed for the Commission's consideration. While I am not attached to any single duration (180 days? 240? 365?) of any limitation, I do not find it unreasonable to expect the Commission to act in a time frame consistent with Congress' view as to the need for timely and predictable action.

As to the rest of section 401, which expands the Commission's merger authority in certain respects, I add my skepticism as to the need for Commission authority to consider the effect of any proposed merger on retail markets. This extension of authority appears to be counterproductive to the goal of more expeditious action on merger applications. The Commission has made it clear that it will consider the effect of a merger on retail competition if the applicable state commission articulates that it is without jurisdiction or lacks the ability to consider such retail competitive effects. In recent years, however, state commissions have refrained from asking the Commission to intercede in this area, and have demonstrated that they are quite competent to address the retail implications of proposed utility mergers. I see no reason to add an additional layer of regulatory review.

Regional Transmission Organizations

I find much to appreciate in section 103 of H.R. 2944, dealing with regional transmission organizations. Specifically, I appreciate its reference to encouraging utility innovation and individual design in the formation of RTOs. But I am deeply concerned by a mandate that compels filings by all utilities by January 1, 2002 and RTO participation by January 1, 2003.

I believe that the Commission already possesses sufficient authority under existing law to encourage transmission-owning utilities to cooperate voluntarily with their neighbors to advance regional solutions to lingering competitive and operational problems in wholesale power markets. I would much prefer to allow utilities to continue the rapid pace of utility restructuring, and to work out among themselves and with their customers—with encouragement from the Commission or Congress rather than a legal directive—how best to design regional markets that serve all interests in an efficient and competitive manner.

The vast majority of transmission-owning utilities already are members of regional transmission institutions (in California, New England, New York, the Mid-Atlantic, the Midwest and most of Texas) or are actively engaged in discussions to form some such type of institution. These developing regional institutions are taking several different forms (most notably, for-profit transcos that own and operate transmission facilities, or not-for-profit independent system operators that do not own the facilities under their operational control). I support Congressional and Commission action that works to encourage this type of regional cooperation—especially with transmission-owning utilities that currently are not "public utilities" subject to the Commission's regulation and oversight. I suspect that transmission-owning utilities increasingly will find it difficult, from many different perspectives (reliability, business, etc.), to refrain from such cooperation. But I do not support Congressional or Commission action that, whether phrased subtlely or more overtly, makes the decision for utilities to turn over operational control of the transmission facilities they own to someone else.

For all of these reasons, I believe that a mandate to join a RTO by a date certain is unnecessary and ill-advised. In my judgment, the other provisions of section 103 give transmission-owning utilities all of the incentive they need to participate in a RTO of their choosing. For example, the section on RTO independence (revised FPA section 202(h)(2)(A)) would afford utilities the discretion to design organizational structures that would allow market participants to retain passive, non-voting interests in the RTO, or own up to 10 percent of the voting interests in the RTO. This provision would allow for a great deal of innovation and flexibility among different types of RTOs in different regions of the country.

Moreover, I support initiatives of the type found in revised FPA section 202(h)(6), which would encourage the Commission to confer "incentive transmission pricing policies" on transmission-owning utilities which decide to participate in RTOs. If Commission-designed encouragement is sufficient, I doubt many utilities would be

able to resist the type of incentive-based pricing policies that would operate as a lure to RTO entry.

Reliability

As I have already explained, competition cannot be at the expense of reliability. Historically, the critical matter of protecting the integrity of the electrical grid has been left in the first instance to the industry itself. The Commission has interceded when necessary to "keep the lights on" or, in recent years, to ensure that reliability-based operating practices do not interfere with the availability or quality of non-discriminatory open access transmission service.

I have been very impressed with the efforts of the North American Electric Reliability Council and the regional councils NERC administers to ensure the continued integrity and reliability of the electrical grid. The electric utility industry and the customers it serves are in a much better position to assess and ensure the continued reliability of electric service than federal regulators lacking intimate familiarity with the details and complexities of remote transmission paths.

I have refrained from calling out for additional regulatory authority over reliability. Nevertheless, as wholesale power markets become increasingly competitive, and strains are imposed on the continuing reliability of the electrical grid planned and designed for a less competitive, more vertically-integrated environment, close cooperation with reliability organizations becomes imperative. For this reason, I have no objection to the language found in section 201 of H.R. 2944 that would clarify the Commission's oversight role by directing it to approve the formation and governance of a "self-regulating electric reliability organization" (ERO). Nor do I object to the Commission's review of mandatory reliability standards and its appellate-type review of implementation and enforcement disputes.

In addition, as electricity markets become increasingly competitive, close cooperation with state and local regulatory authorities with oversight over the reliability of local distribution facilities become imperative. For this reason, I have no objection to the language found in section 201 that would clarify the authority of states and local authorities to ensure the reliability of local distribution facilities. Because I am generally wary of additional layers of regulatory review that may add to uncertainty, I am very appreciative of the language of revised section 217(n) of the FPA that ensures that such authority would not be exercised in a manner that could impair the reliability of bulk power systems.

My only hesitation with respect to the reliability provisions of H.R. 2944 would be the Commission's ability to entertain a much larger share of reliability-based issues and disputes, as envisioned in section 201, in light of its limited resources and general unfamiliarity with these issues (which might have to be decided in close to "real-time"). My hope is that the need for Commission intervention will be lessened by increasing respect for the mandatory rules of the EROs the Commission approves. And the availability of "incentive transmission pricing policies", referenced in section 103 of H.R. 2944, limited to transmission-owning participants in RTOs that act to promote reliable transmissions operations and encourage investment in and expansion of transmission facilities, should act as a significant incentive to minimize any reliability-based disputes.

Federal/State Jurisdiction

Finally, I am pleased to see legislative language in section 101 of H.R. 2944 that clarifies the now-murky boundaries between federal and state jurisdiction over different aspects of electricity supply and delivery. The clarifying language, for the most part, adopts the jurisdictional dividing lines adopted by the Commission in its Order No. 888 rulemaking; those lines, for the most part, have been accepted by industry participants and state regulatory commissions. I believe it is important, whenever possible, to eliminate jurisdictional turf battles and protracted court disputes over ambiguous congressional delegations, in order to ensure that the benefits of increased competition flow through to consumers as quickly and comprehensively as possible.

In light of recent litigation on the subject of comparability of service, I would add one more clarification. That addition would clarify that the Commission's jurisdiction over unbundled transmission service is exclusive, and that the Commission retains the authority to protect against undue discrimination or preference in the provision of transmission service to all transmission users. Such clarification would codify existing Commission policy by allowing it to require that a transmission-owning utility offer transmission service to others that is comparable to (i.e., no worse than) the service it provides to itself.

Thank you for the opportunity to present my views on this important piece of federal legislation. I am happy to answer any questions you now may have.

Mr. BARTON. Thank you, Commissioner.

Before we recognize Commissioner Breathitt, I want to remind the other commissioners we do have all your statements in their entirety in the record, and I think most of the subcommittee have read them.

The Chairman did an excellent job of summarizing within a reasonable time. Commissioner Bailey's remarks were well taken, but they took about 15 minutes. So, the other three commissioners, we don't want to constrain you, but we hope that you could summarize in 5 to 10 minutes.

Ms. Breathitt.

STATEMENT OF HON. LINDA KEY BREATHITT

Ms. BREATHITT. Thank you, Mr. Barton. I do admit that I am a Southerner, and I might talk a little slower, but I do have a summary of my testimony, and it is four double-spaced pages.

Good afternoon, and I do sincerely thank you for inviting me and my colleagues to appear before you today to discuss the need for Federal electricity legislation and the provisions of H.R. 2944.

Let me begin by commending you, Mr. Chairman, and other members of the subcommittee and your staffs, for crafting what I consider to be a comprehensive and important piece of legislation that certainly has gotten the attention of virtually everyone in the electric industry, including the administration and State and Federal regulators. The efforts of this committee have advanced the level of electricity discussion, and that is a good thing.

I believe that Federal electricity legislation, such as H.R. 2944, is needed to address the uncertainty that seems to exist in the industry. Much of the uncertainty surrounds issues such as statutory authority, jurisdiction, and the need for and effect of wholesale and retail competition. The guidance and clarification offered by the legislation will enable the Commission to further its goals of achieving a fair, open, and competitive bulk power market.

My written testimony addresses 5 specific aspects of the legislation, and this afternoon I would like to briefly summarize these.

The first is open access transmission. The Commission has worked diligently for several years to open the Nation's electric transmission system for the provision of non-discriminatory transmission service to all wholesale buyers and sellers. However, certain impediments to full open access remain, and I believe that section 102 of the bill addresses one of those impediments by providing the Commission authority to require open access transmission on the part of State and municipal utilities and rural electric cooperatives. Many of these entities have already filed open access reciprocity tariffs with FERC, and I believe this provision would result in a more cohesive transmission grid and will greatly facilitate open access.

The second issue is regional transmission organizations, which we have come to call RTOs. On May 13, in a unanimous decision, the Commission issued its Notice of Proposed Rulemaking on RTOs. The Commission found that RTOs would beneficially address many of the operational and reliability issues now confronting the industry. In the NOPR, the Commission sought to ac-

complish its objective of forming RTOs by strongly encouraging voluntary participation by public utilities.

The voluntary approach for RTO formation outlined in the NOPR was, in my opinion, a fundamental aspect of our proposal. Section 103 of the bill would require all utilities to join an RTO by a certain date. I continue to prefer the voluntary approach at this time and believe there is considerable support among stakeholders for a voluntary approach. And, as Chairman Hoecker just said, we do agree that RTOs can bring many benefits to competitive markets.

The third issue is expansion of the interstate transmission facilities. One of the most important issues facing the electric industry is the need to enhance or expand the transmission grid. Section 105 of the bill proposes to address this by authorizing the Commission to rule on applications filed by transmitting utilities to expand facilities after consultation with regional joint boards comprised of effective State and Federal agencies. Because certificate authority does reside with the States, I believe a FERC role would be confusing, although I support regional cooperative efforts.

The fourth issue is electric reliability. Section 102 of the bill would provide the Commission with authority pertaining to the formation of a self-regulating electric reliability organization and the development of enforceable reliability standards. I believe that emerging competition in the electric industry necessitates a change in the manner in which the reliability of the grid is overseen and managed, and I believe that the current system should be replaced by a model similar to that proposed in the bill.

And the final issue that I address in more detail in my written testimony is merger authority. Section 401 of your bill authorizes the Commission to review proposed mergers of facilities of all electric utilities, including State and municipal utilities, rural cooperatives, and Federal electric utilities. This section also extends the Commission's merger authority to include generation companies.

I support the provisions of this section. I believe the Commission is uniquely situated and eminently qualified to perform this important task. Given the changing nature of the industry, I believe it is essential that the Commission continues to evaluate utility mergers and that the scope of our merger authority be extended as you have proposed.

Furthermore, I believe the proposed time limit proposed in the bill is reasonable but should be modified to allow the Commission additional time to review in a public hearing context the occasional merger application that raises issues of material fact.

In conclusion, let me again commend this subcommittee for crafting an important bill. I appreciate this opportunity to share my thoughts, and I will look forward to your questions.

[The prepared statement of Hon. Linda Breathitt follows:]

PREPARED STATEMENT OF LINDA BREATHITT, COMMISSIONER, FEDERAL ENERGY REGULATORY COMMISSION

Chairman Barton and Members of the Subcommittee: Good morning. My name is Linda Breathitt and I am a Commissioner of the Federal Energy Regulatory Commission. Thank you for inviting me and my colleagues to appear before you today to discuss the need for Federal electricity legislation and the provisions of H.R. 2944, the Electricity Competition and Reliability Act of 1999.

Let me begin by commending you, Mr. Chairman, and other Members of the Subcommittee for crafting what I consider to be a comprehensive and important piece

of legislation that will certainly advance the development of competitive wholesale and retail electricity markets in this country.

I believe that Federal electricity legislation, such as H.R. 2944, is needed to address the uncertainty that seems to exist in the industry. Much of the uncertainty surrounds issues such as statutory authority, jurisdiction, and the need for and affect of wholesale and retail restructuring. I believe H.R. 2944 will, in large part, allay the uncertainty. Furthermore, the guidance and clarification offered by the legislation will enable the Commission to further its goals of achieving a fair, open, and competitive bulk power market.

I am unable today to address each provision of H.R. 2944. Therefore, I would like to comment briefly on five specific aspects of the proposed bill: (1) open transmission access; (2) regional transmission organizations; (3) expansion of interstate transmission facilities; (4) electric reliability; and (5) merger authority.

Open Transmission Access

The cornerstone of the Commission's efforts to create an open, non-discriminatory electric transmission system is the requirement that all public utilities that own, operate, or control interstate transmission facilities provide transmission service over their facilities to all wholesale buyers and sellers on a non-preferential basis. Such non-discriminatory open access to transmission services is essential to the development of competitive wholesale bulk power markets. Despite the Commission's efforts, however, certain impediments to full open access remain. One such impediment is that a significant portion of the Nation's transmission grid is owned and operated by utilities not subject to Commission open access requirements. Section 102(b) of H.R. 2944 amends the definition of "public utility" in section 201(e) of the Federal Power Act (FPA) to include transmitting utilities, other than Federal power marketing administrations and the Tennessee Valley Authority, for purposes of regulating transmission rates, terms, and conditions. I believe this provision would result in a more cohesive transmission grid and will greatly facilitate open transmission access.

Regional Transmission Organizations

On May 13, 1999, in a unanimous decision, the Commission issued its Notice of Proposed Rulemaking (NOPR) on Regional Transmission Organizations (RTOs). In the NOPR, the Commission found that appropriate regional transmission institutions can address many of the operational and reliability issues now confronting the electric industry. Specifically, we found that such institutions could: (1) improve efficiencies in transmission grid management; (2) improve grid reliability; (3) remove the remaining opportunities for discriminatory transmission practices; (4) improve market performance; and (5) facilitate lighter handed regulation.

The Commission proposed, among other things, to establish fundamental characteristics and functions that RTOs must satisfy. Furthermore, we proposed that all public utilities that own, operate, or control interstate transmission facilities make certain filings pertaining to participation in an RTO. Specifically, utilities not already participating in an approved Independent System Operator (ISO) would make one of two alternative filings with the Commission by October 15, 2000. First, a utility may propose to participate in an RTO that satisfies the minimum characteristics and functions and that will be operational no later than December 15, 2001. Alternatively, a utility may make a filing that describes its efforts to participate in an RTO, any existing obstacles to RTO participation, and any plans and timetables for future efforts to participate in an RTO. A public utility that is already a member of an existing ISO would make a filing no later than January 15, 2001 that explains, among other things, the extent to which the ISO in which it participates meets the minimum characteristics and functions for an RTO.

In the NOPR, the Commission sought to accomplish its objective of forming RTOs by encouraging voluntary participation by public utilities. In this light, as indicated above, the Commission proposed, as part of its filing requirements, a process for a utility to describe in an alternative filing any efforts to participate in an RTO, reasons it has not participated in an RTO, any obstacles to RTO participation, and any plans the public utility has for further work toward participation in an RTO.

The voluntary approach for RTO formation outlined in the NOPR is, in my opinion, a fundamental and crucial aspect of our proposal. I believe that a certain amount of flexibility is necessary on the part of the Commission as utilities move toward forming RTOs. Therefore, it is important to me that public utilities have an opportunity to identify and explain any obstacles or restrictions they face in joining an RTO.

Section 103 of H.R. 2944 would require all transmitting utilities to establish or join an RTO by January 1, 2003. I believe that Congress should not impose, at this

time, a mandate for utilities to join an RTO, but rather should encourage voluntary participation. There is considerable support among stakeholders for a voluntary approach.

Section 103 of H.R. 2944 also proposes certain standards that RTOs must meet. In his testimony to the Subcommittee today, Commission Chairman James J. Hoecker recommends that Congress take a somewhat different approach. Given that the Commission has yet to evaluate all of the comments submitted on its RTO NOPR, Chairman Hoecker suggests that Congress should not lock the details of these standards into statutory text given the possible need to adapt the standards to future changes in the industry before the FPA is again modified. I agree with Chairman Hoecker that Congress should preserve the Commission's discretion to reflect changing circumstances in specific RTO requirements and standards.

Expansion of Interstate Transmission Facilities

One of the most important issues now facing the electric industry is the need to enhance or expand the transmission grid. The success of the Commission's goals of transmission open access and wholesale competition depends on an adequate and reliable supply of transmission capacity. Since the issuance of Order No. 888 in 1996, there has been a tremendous increase in the amount of wholesale electric power being traded. Open access and industry restructuring, both at the wholesale and the retail levels, have caused demand for transmission capacity to soar. As a result, the Nation's transmission grid is struggling to keep pace with the industry's rapid growth. The increased usage is imposing tremendous strain on the system. The Commission must take deliberate action to encourage the industry to address this situation.

Section 105 of H.R. 2944 proposes to address grid expansion by authorizing the Commission to order a transmitting utility to expand its transmission facilities, upon application of an electric utility or transmitting utility. Furthermore, this section would create joint boards consisting of State and Federal agencies to make recommendations to the Commission pertaining to transmission system expansion. In his testimony, Chairman Hoecker states that he sees no compelling need for the Commission to be given the authority specified in Section 105 of H.R. 2944. I agree with Chairman Hoecker on this point. It is my belief that RTOs will play a significant role in system expansion.

In my opinion, the transmission system is not keeping pace with growing demand in the bulk power market. The reason for this is that the industry is increasingly unwilling to make transmission-related investments given the uncertainties that exist in an industry still in the midst of restructuring and the risk of earning inadequate returns on new transmission investments. I believe the Commission must address this problem in two ways. First, the Commission must ensure that its transmission pricing policies conform to the changing electricity marketplace and that transmission owners or operators are encouraged to file innovative pricing proposals. Second, the Commission must adopt policies that will provide proper incentives to market participants and other investors to expand and enhance transmission facilities. Both of these objectives will be addressed, as they pertain to RTOs, at least, in the new FPA section 202(h)(6) as proposed in section 103 of H.R. 2944. This would be a reasonable starting point for the Commission to consider the effect its current transmission pricing policies have on the evolving electric industry and the need for a more incentive-based approach.

Electric Reliability

Section 201 of H.R. 2944 amends the FPA to provide the Commission with specific authority pertaining to the formation of a self-regulating electric reliability organization and the development of enforceable reliability standards. Many in the industry, including the North American Electric Reliability Council (NERC), recognize the lack of clear Federal authority for establishing or enforcing reliability standards for the electric industry and the importance that electric reliability be maintained as the industry is restructured. I believe that emerging competition in the electric industry necessitates a change in the manner in which the reliability of the interconnected electric system is overseen and managed. The present model of voluntary compliance by electric utilities of regulatory rules and criteria established by NERC and its member Regional Reliability Councils has worked effectively for over three decades. However, given the profound changes taking place in the industry, I believe this voluntary system should be replaced by a model similar to that proposed in Title II of H.R. 2944. Such a model would retain many of the features of the current system that has been so effective in the past, while adding necessary oversight and enforcement mechanisms. There is a compelling need for such Federal authority and I support the provisions of this section.

Merger Authority

Section 401 of H.R. 2944 amends the FPA to authorize the Commission to review proposed mergers and disposition of facilities of all electric utilities and transmitting utilities, including State and municipal utilities, most rural electric cooperatives, and Federal electric utilities. This section extends the Commission's merger authority to include generation companies and clarifies the Commission's merger authority over holding companies. Furthermore, the section establishes time limits for the Commission to review merger applications.

I support the provisions of this section. The Commission is charged under Section 203 of the FPA to evaluate public utility mergers and dispositions to determine whether such actions are consistent with the public interest. I believe the Commission is uniquely situated and eminently qualified to perform this important task. The Commission and its Staff possess extensive knowledge of and expertise in the electric industry. Given the changing nature of the electric industry, I believe it is essential that the Commission continues to evaluate public utility mergers and that the scope of our merger authority be extended as proposed in this section.

As for the time line proposed in section 401(a)(4) of H.R. 2944, I believe the Commission has shown repeatedly that it processes merger applications within the prescribed 150-day period. However, I agree with Chairman Hoecker that occasionally a proposed merger raises issues of material fact that must be resolved in a public hearing context. In these instances, I believe the Commission would need additional time in which to process the application.

Conclusion

In conclusion, I believe that Federal legislation is needed to address uncertainty that exists in the industry. For the most part, I believe that H.R. 2944 accomplishes this objective. However, there are certain provisions of the proposed legislation that should be revised. I have identified a few such instances.

Congress has a considerable opportunity in this session to pass meaningful legislation that will expand competition in the wholesale and retail electric markets. I urge Congress to avail itself of this opportunity. I look forward to continuing the dialogue with the Subcommittee on this important legislation.

Mr. BARTON. Thank you, Commissioner.

We would now like to hear from Commissioner Hebert.

STATEMENT OF HON. CURT L. HEBERT, JR.

Mr. HEBERT. Thank you for the opportunity to appear before you today. Chairman Barton's invitation specifically asked me to address whether there is a need for Federal electricity legislation, and, if so, why?

In the interest of time, I have modified my comments, and I ask and answer a more narrow question: Does FERC need Federal electricity legislation? Not necessarily.

For investor-owned utilities, FERC has adequate existing authority to create a competitive market; more accurately, I should say allow a competitive market to form. One area Congress could speak to involves the Federal power marketing agencies—the Bonneville Power Administration and the Tennessee Valley Authority. The effort involves untangling the transmission from the generation and the financial and legal commitments these agencies may have made. Change also involves the matter of tax exempt financing and the problem of preference customers and the so-called fence within which bodies, such as TVA, operate. Therefore, it will take time to sort out. I would prefer selling off their transmission assets instead of additional jurisdiction.

For the investor-owned side, the economics of the industry already push companies into restructuring. Generation now operates as a true business. FERC has extended market-based rates from merchant generators to services traditionally provided by utilities. In Order Number 888, the Commission declared new entry into

generation will receive market-based rates for all practical purposes. Transmission, the highway of electricity, will remain regulated and will operate as a utility.

The next step must come from Federal Energy Regulatory Commission. Our rate setting encourages utilities to sit still and do nothing. We all but prohibit companies from engaging in the transmission business. We also keep new investors out. In allowing utilities to recover original cost, less depreciation on facilities about 30 years old, FERC says to a potential entrant, ''You cannot afford to buy these facilities for their value.'' It also tells integrated utilities, ''You won't get anything for your assets, so if you sell, you will be asking for shareholder opposition.''

To cure that, FERC must grant an acquisition adjustment that reflects the economic benefits transmission facilities will bring to the table. On the other hand, policies that force sellers to return ratepayers any and all gains from a sale negate the good in the acquisition adjustment. FERC and the states must allow shareholders to reap at least half the profits of the sale of transmission. FERC can do this.

Higher rates of return to reflect greater risk of transmission would encourage restructuring for existing facilities, as would shorter depreciation to account for the likelihood of distributed generation and other technological changes that may render facilities obsolete before the end of their physical life. FERC can do this.

Most important for the future, restructuring, competition, and innovation come down to expansion. Business has a simple way of handling new facilities—incremental pricing. Arbitrary as it might seem from a theoretical point of view, making the new customer pay the cost of the interconnection brings certainty at the least cost. Existing customers can rest assured, once they have paid their freight, that a new customer would not saddle them with more.

All of this and more FERC can accomplish by exercising its authority under Section 205 of the Federal Power Act. Since the 1940's, the Supreme Court has held that nothing in the act binds the Commission to any particular formula, as long as we balance the interests of consumers with that of the utilities. Were we to do that here, we would institute the kinds of incentives and performance-based rates that will allow a separate transmission business to form and thrive. A separate transmission business, a clean break, in the words of the Federal Trade Commission staff's comments in the RTO NOPR, forms the best foundation for competition in generation and low prices to the customer.

Other impediments to restructuring exist, some of which you correctly blame FERC for, even apart from rates. For example, utilities complain that FERC takes too long to rule on applications to dispose of facilities, of the type that utilities will have to file in order to form RTOs. Congress, in theory, can legislate an end to delay. Better yet, FERC itself can and should accelerate the process.

I think we should put a provision into the Final RTO Rule that we will act on those applications within 6 months. FERC should use its existing discretion. FERC's review of mergers could delay formation of RTOs.

The current draft of the Barton bill in front of us today, that we are speaking about, expands FERC's jurisdiction over mergers by including generating facilities. The August 4 draft would have eliminated FERC review of mergers. FERC should get out of the merger business. I have always said good mergers should be approved in 6 months, and bad mergers should never happen. Utilities are not exempt from the antitrust laws of this great Nation. DOJ, FTC, the SEC all take a look—FERC is not an antitrust agency.

We hear clamor in another area: reliability. The argument goes that competition, meaning cost shifting—or cost cutting, excuse me, will slight the long-term investment in reliability. Therefore, critics caution, Congress must step in. I disagree completely, that the two considerations must pull in different directions. Here, again, FERC has authority to act.

We can supplement performance-based rates to include reliability, another word for quality. When I served as commissioner and chairman in Mississippi, we included the minimum reliability as one measure of performance on which the utilities can earn profit. We at the FERC could adopt the same measure as part of the rate plans under section 205 of the Federal Power Act. Adding reliability to performance-based plans means quicker action than having a self-regulating organization establish standards with appeals to FERC, because we would make the utility's economic interest coincide with the public interest. Here, again, FERC has the existing authority to act.

I noted with approval of the reports that this draft of the bill rejects FERC's mandates and favors incentives. When I read the draft, I saw that in fact the authority for FERC to mandate RTOs fell away, and the bill directs FERC to offer incentives. So far, so good.

I pause, however. Under the draft bill, Congress, not FERC, mandates RTOs. For the industry, a mandate robs companies of the initiative, whether the compulsion comes from a law or from an administrative rule. Moreover, the draft requires FERC to consider existing transmission organizations in certifying RTOs. This prevents progress. The most ardent advocates of existing ISOs concede that these organizations represent, at best, a step toward the ultimate goal of true independence. In short, everyone agrees ISOs must evolve. This bill freezes the status quo with existing ISOs. I would allow ISOs to exist, though I find them falling short of the RTO criteria of independence. Instead, I would clear the way toward the goal: truly independent transmission companies.

This leads to my next topic, incentives. Everyone knows I favor them. To work effectively, however, incentives must induce, not sugar coat compulsion. If Congress mandates RTOs, at best, you turn precisely designed economic measures that proponents must tie to specific results into rewards for obeying the law. At worst, you rob incentives of their meaning. We must ask ourselves: Does the seller to a distress sale really negotiate the price?

Companies deserve no reward for obeying the law. I wonder how we would design proper incentives for past or even existing conduct. Since ISOs must evolve into better organizations, we should provide the incentive only for the better organizations. You could

solve the problem by inserting a sunset date for ISOs to become truly independent. Once we freeze ISOs as the preferred institutions, we have stopped in its tracks the evolution of the industry.

I did want to comment on something that Deputy Secretary Glauthier said in regard to incentives and RTOs. He said—and I am pretty sure it was within one sentence—that we don't need incentives and that utilities will join RTOs on their own and that mandates are needed. Well, those are three different things, and they can't all be true, because you either need incentives or you need mandates or everyone joins voluntarily.

And let us not forget how we did solve some of our Clean Air Act problems. The SO_X and NO_X credit showed incentives worked gracefully and wonderfully are working today, and I insist we rethink that in the electricity area.

We must treat transmission as a business. Regulation treats transmission as politics with committees, debates, and compromises, and as law with complaints, litigation, and appeals. Treating transmission as a business means rescinding regulations that prevent business people from operating transmission as a viable enterprise. Your predecessors gave FERC broad authority to establish just and reasonable rates. The courts have given deference to our expertise. Let us use that tool, and let competition flourish. In short, let FERC let go.

Over the last 2 years we have changed the debate from historical regulatory prescription and mandate to that of empowerment through economic persuasion. Since you are seeking my counsel, I will be a bit more bold than usual. I do need the help of Congress. I have made it clear to the members of this committee on the occasion I have had to speak with them that your intentions are not clear at the Federal Energy Regulatory Commission. I have invited oversight and believe this to be a step in the right direction. You and your predecessors have given us the right tools. I need you to ensure they are being used properly.

Thank you, and, Mr. Chairman, I do apologize if I went a little longer than expected. Myself and Commissioner Bailey are not accustomed to being in the majority.

[The prepared statement of Hon. Curt L. Hebert, Jr. follows:]

PREPARED STATEMENT OF HON. CURT L. HEBERT, JR., COMMISSIONER, FEDERAL ENERGY REGULATORY COMMISSION

Thank you for the opportunity to appear before you. Chairman Barton's invitation specifically asked my colleagues and me to address "whether there is a need for Federal electricity legislation, and if so, why . . .". The letter also requested comment on specific provisions of the Barton Bill and solicited alternate language, if possible.

I have publicly stated on many occasions that I will comment on the need for legislation only if asked. Since, Mr. Chairman, you have done so, I will give you my views to the full extent of my thinking, as it pertains to FERC. I will comment in general on certain provisions in the Bill and will not presume to propose alternate language, as I have had but a few days to read this massive Bill. I will, of course, gladly go into detail in response to questions.

Does FERC need Federal electricity legislation? Not necessarily. For investor owned utilities, FERC has adequate existing authority to create a competitive market. More accurately, I should say allow a competitive market to form. Enough authority at the state level exists to allow competition to spread there and to include publicly owned utilities.

The one area Congress could speak to involves the Federal power marketing agencies, the Bonneville Power Administration and the Tennessee Valley Authority. While I think it desirable to cover that part of the picture, I think Congress can

wait until the rest of the country sorts out its restructuring and the affected regions, the Northwest, Southwest and Southeast, have an opportunity to consider the complex issues. The effort involves untangling the transmission from the generation and the financial and legal commitments these agencies may have made. Change also involves the matter of tax exempt financing and the problem of preference customers and the so-called "fence" within which bodies, such as TVA, operate.

For the investor owned side, the economics of the industry already push companies into restructuring. Generation now operates as a true business. FERC has extended market based rates from merchant generators to services traditionally provided by utilities. In Order No. 888, the Commission declared new entry into generation will receive market based rates, for all practical purposes. Transmission, the highway of electricity, will remain regulated and will operate as a utility.

As we saw in other industries, beginning with the airlines, a business and a utility use opposite approaches. A CEO of a business looks at value, innovation and opportunity; a CEO of a utility looks at cost, rate base and rate of return. In visits to my office, officials of integrated utilities have expressed the desire to tackle one or the other—looking for profits in generation or engaging in strategically important transmission. Witness as well some utilities, such as Duke Energy and the Southern Company, buying generation that others, such as New England Power Company and Consolidated Edison Company, sell off. As I wrote in an article in the *Public Utilities Fortnightly* last year, "The fruit of divestiture has ripened."

The next step must come from FERC. Our rate setting encourages utilities to sit still. We all but prohibit companies from engaging in the transmission business. We also keep new investors out. In allowing utilities to recover original cost, less depreciation on facilities about 30 years old, FERC says to a potential entrant, "You cannot afford to buy these facilities for their value." It also tells integrated utilities, "You won't get anything for your assets, so if you sell, you will be asking for shareholder opposition." To cure that, FERC must grant an acquisition adjustment that reflects the economic benefits transmission facilities will bring to the table. On the other side, policies that force sellers to return to ratepayers any gains from a sale negate the good in the acquisition adjustment. FERC and the states must allow shareholders to reap at least half the profits from sale of transmission.

Higher rates of return to reflect greater risk of transmission would encourage restructuring for existing facilities, as would shorter depreciation to account for the likelihood of distributed generation and other technological changes that may render facilities obsolete before the end of their physical life.

Most important, for the future, restructuring, competition and innovation come down to expansion. We have all seen statistics showing transmission investment has declined to a trickle (if not less). Primarily, a pricing scheme that requires all customers to pay for all facilities creates arguments. It leads to controversies. Why should I, an existing customer, pay for a new line, when I have all I need? On the other side, I, as a new customer, want everyone else to supplement my costs, so of course, everyone should contribute to my line!

Business has a simple way of handling new facilities: incremental pricing. Arbitrary as it might seem from a theoretical point of view, making the new customer pay the entire cost of interconnection brings certainty at the least cost. Existing customers can rest assured, once they paid their freight, that a new customer would not saddle them with more. New customers will have to calculate the full cost of their ventures and will plan accordingly. Once they commit to a price, they will see the transaction through. I add here, parenthetically, that incremental pricing will still leave some controversy, when opposition to construction or upgrade stems from other considerations.

All of this, and more, FERC can accomplish by exercising its authority under Section 205 of the Federal Power Act. Since the 1940's, the Supreme Court has held that nothing in the Act binds the Commission to any particular formula, as long as we balance the interests of consumers and utilities. Were we to do that here, we would institute the kinds of incentives and performance based rates that will allow a separate transmission business to form and thrive. A separate transmission business, a "clean break," in the words of the Federal Trade Commission Staff's comments in the RTO NOPR, forms the best foundation for competition in generation and low prices to the customer.

Other impediments to restructuring exist, some of which you correctly blame FERC for, even apart from rates. For example, utilities complain that FERC takes too long to rule on applications to dispose of facilities, of the type that utilities will have to file in order to form RTOs. Congress, in theory, can legislate an end to delay. Better yet, FERC itself can and should accelerate the process. I think we should put a provision into the Final RTO Rule that we will act on those applications within six months. FERC should use its existing discretion. Moreover, the Au-

gust 4th draft would have eliminated FERC review of mergers. Currently, FERC's review of mergers could delay formation of RTOs. The August 4th draft had a good idea.

We hear clamor in another area: reliability. The argument goes that competition, meaning cost cutting, will slight the long-term investment in reliability. Therefore, critics caution, Congress must step in. I disagree completely that the two considerations must pull in different directions. I also disagree completely that Congress must take the lead. Here, again, FERC has authority to act.

Remember, in a business, the management looks at profit margins, not low cost. Earning a profit entails quality service; or, more accurately, several layers of quality service, depending on how much the consumer wants to pay. In any event, entrepreneurs must meet minimum criteria. In most instances, take electric appliances, for example, a close relative to the electric industry, Underwriters Laboratory, a private group, sets standards that companies adhere to without the need for one word of legislation. Why? Society makes it in the interest of appliance manufacturers to do so.

We can supplement performance based rates to include reliability, another word for quality. When I served as a Commissioner and Chairman in Mississippi, we included the minimum reliability as one measure of performance on which the utilities earned profit. We at the FERC could adopt the same measure as part of rate plans under section 205 of the Federal Power Act. Adding reliability to performance based plans means quicker action than having a self-regulating organization establish standards with appeals to FERC because we would make the utility's economic interest coincide with the public interest. Here, again, FERC has existing authority to act.

Furthermore, taking the regulatory approach makes meeting the goal more difficult. Coercion means utilities would resist, at the Commission and in the courts of appeals. If we compensate companies for their additional risk taking and bold action, we align the economic interest and the public interest. We would not need to discuss authority for FERC or legal issues of the type this hearing will debate. Again, as I wrote in my article, "FERC must let [the ripe fruit] fall from the tree."

I said at the outset of this testimony that existing institutions can deal with municipal utilities and cooperatives. Having served in the Mississippi Legislature, I know that cities, counties and districts exist as creatures of the state. Under the Mississippi Constitution, as in other states, the Legislature exercises tight control over the affairs of political bodies within its boundaries. The Legislature must authorize taxes and expansion of municipalities into new areas. With that leverage, state legislatures can enact laws to place public transmission agencies on the same track as investor owned. FERC, of course, might think it can do it too, and, under the Barton Bill, we would have the jurisdiction. I think, however, that the elected legislatures, closer and more accountable to the people, know better than FERC, how to accomplish restructuring in their areas. The August 4th draft directed the FERC to give "maximum practicable deference" to state commissions, which would be preferable to mere deference. After all, we all agree that low prices to the customer remains the paramount end. Restructuring forms but a means to that end.

I see no need for legislating on the cooperatives. The strong economy and changes in the law give cooperatives incentives to pay off their debts to the Rural Utilities Service. If this trend continues, as we have seen at FERC, many will become public utilities under FERC regulation. If FERC enacts incentives for transmission, more will volunteer. In this market of deregulated generation, cooperatives and municipals, with their local roots, will see their niche as serving the people's need for transmission. I do not think that they could compete nationally as generators with the large investor owned companies. As I have said repeatedly, if FERC incents, they will come. I think the municipals and cooperatives will, too.

Now I will turn what, to me, form the major features of the Bill: incentives and flexibility. The approach the proposed legislation takes holds great interest to me. From the beginning of my tenure at FERC, I have spoken out forcefully in favor of encouragement and incentives and against mandates. Even with my vision of an independent transmission company as the model for RTOs, I favor allowing other forms of organizations to exist. I would just give incentives to RTOs that exhibit true independence.

I noted with approval the reports that this draft of the Bill rejects FERC mandates and favors incentives. When I read the draft I saw that, in fact, the authority for FERC to mandate RTOs fell away, and the Bill directs FERC to offer incentives. So far, so good.

The fine, print, however, makes me wonder about the direction the Bill is heading. Section 103 requires all transmitting utilities to establish or join an RTO, albeit of their own design by 2003. Paragraph (2) establishes criteria and wisely says that

independence encompasses separation of control, but could include passive ownership and 10% voting control or lower. I agree with the idea that independence requires separation of legal control and tolerate passive ownership and 10% voting control. I acknowledge that 2003 extends by almost one year the deadline the RTO NOPR has for voluntary RTOs to begin operation.

I pause, however. Under the draft Bill, Congress, not FERC, mandates RTOs. For the industry, a mandate robs initiative, whether the compulsion comes from a law or from an administrative rule. Moreover, the draft requires FERC to consider existing transmission organizations in certifying RTOs. This prevents progress. The most ardent advocates of existing ISOs concede that these organizations represent, at best, a step toward the ultimate goal of true independence. In short, everyone agrees ISOs must evolve. This Bill freezes the *status quo* with existing ISOs. As I said at the outset, I would allow ISOs to exist, though I find them falling short of the RTO criterion of independence. Instead, I would clear the way toward the goal: truly independent transmission companies.

This leads to my next topic, incentives. Everyone knows I favor them. To work effectively, however, incentives must induce, not sugar coat compulsion. If Congress mandates RTOs, at best, you turn precisely designed economic measures that proponents must tie to specific results into rewards for obeying the law. At worst, you rob incentives of their meaning. We must ask ourselves, does the seller to a distress sale really negotiate the price?

Although I support incentives as providing proper direction and motive, I oppose an indiscriminate application of incentives. The draft Bill requires incentives for existing ISOs, rewards they do not need and that I would deny them. I said earlier exiting ISOs fail the independence test. Besides that, why increase rates for past conduct that occurred anyway? Some of the past conduct occurred under the compulsion of law. Companies deserve no reward for obeying the law. I wonder how to design proper incentives for past conduct. As with grandfather provisions for existing ISOs as RTOs, giving the same incentives to ISOs defeats the purpose of restructuring. Since ISOs must evolve into better organizations, we should provide the incentive only for the better organizations. Once we freeze ISOs, we have stopped in its tracks the evolution of the industry.

You could solve the problem by inserting a sunset date for ISOs to become truly independent. The draft Bill has nothing in it. If you wanted to enact something and chose a date (without being arbitrary), you should save the incentives for organizations that get to the end state earlier. On that score, I note that this Bill removed the date for retail competition, a step that I applaud.

If I may, please let me conclude with a discussion of one more provision that I think illustrates the distinction between my approach and that of the draft Bill. I agree with the goal, I raise questions about the means.

The draft Bill enmeshes the government in reliability to a greater extent than now, or necessary. FERC will have to certificate a reliability organization, hear appeals of controversies over reliability and establish mandatory rules. The model for this comes from the Securities and Exchange Commission with self-regulating stock exchanges. I dare say I am not an expert in stocks, but I can see something like that for a market in which unsophisticated and unsuspecting investors may lose their life savings.

Here, however, we have a better solution. We deal with sophisticated businesses. This reality allows for performance based rates as the insurer of reliable operations. Reliability has two components: safety and adequate capacity. Both of these, or the lack of them, affect the bottom line of a business. My suggestion then is to create a climate in which that occurs in transmission. Specifically, tie profits to performance—safe performance and an adequate number of transactions. Give transmission companies business plans to meet. Favorable earnings result from good results, losses from poor management. Clearly, we don't need legislation to do that. FERC has the authority to institute performance based rates. We did it in Mississippi. The Public Service Commission put three criteria into the final plans. Two of them fall directly under the category of reliability, and one indirectly. Earnings depended on the number and duration of interruptions, customer satisfaction (using actual complaints) and price into which we factored sales transactions. The companies figured out how to set and meet reserve margins, safety standards and capacity goals. We aligned the private economic interest with the public interest. FERC can do that now. We said in the RTO NOPR that we would consider it. Why enmesh FERC in details that it has no expertise or resources to devote? Instead of engaging in proceedings lasting years and years debating reserve margins and capacity needs, FERC, every few years, would review performance plans and fine tune them.

Congress should leave it up to FERC to get restructuring right. I think we must treat transmission as a business. Regulation treats transmission as politics, with

committees, debates and compromises and as law with complaints, litigation and appeals. Treating transmission as a business means rescinding regulations that prevent business people from operating transmission as a viable enterprise. Your predecessors gave FERC broad authority to establish just and reasonable rates. The courts have given deference to our expertise. Let us use that tool and let competition flourish. In short, let FERC let go.

Thank you.

Mr. BARTON. Well, I am sure you wrote it for 5 minutes, but you spoke it for about 12 minutes. That is just—but I listen at about the 12-minute speed, so that is okay.

Last but not least, the Honorable Commissioner Massey, and you are recognized for such time as you may consume.

STATEMENT OF HON. WILLIAM L. MASSEY

Mr. MASSEY. Thank you, Mr. Chairman. I will try to be brief, because I am going to endorse in large part many provisions of your bill.

It is my view that the enactment of this legislation with certain amendments can ensure an open, seamless, and highly reliable interstate transmission grid that will in turn facilitate vibrantly competitive power markets.

Why should Congress act now? Simply stated, legislation is necessary to facilitate the removal of barriers that undercut the economic promise of competition. Market and grid access uncertainties that flow from such barriers can stifle investment in necessary generation and exacerbate price volatility. Residual market power, a patchwork of grid rules, or rules followed merely on a voluntary basis, can smother embryonic competitive markets.

Legislation can resolve these uncertainties, and since all power sold at wholesale is ultimately consumed at retail, it is important to understand that efficient wholesale markets are a necessary predicate to efficient retail markets.

Thus it is my view that H.R. 2944's provisions subjecting all transmitting utilities to one set of rules should be enacted. Provisions requiring transmission owners to join RTOs by a date certain, in my judgment, are in the public interest. However, detailed legislative standards for such institutions that may need to evolve over time are unnecessary.

Provisions authorizing the private reliability standards organization to promulgate mandatory rules should be enacted. Under the legislation, the Commission would certify that organization and rely substantially on its expertise. The Commission would not develop the rules but would rely upon the private organization to do so. This is in the public interest.

Market power can smother embryonic competitive markets. I would suggest that H.R. 2944 be amended with language from H.R. 1828 and H.R. 2050 authorizing the Commission to examine and address market power in wholesale and retail markets in certain circumstances.

A recent 8th Circuit Court of Appeals decision sanctions a state policy granting a preference for in-state uses of the interstate grid. It is roughly analogous to a State reserving the interstate highway system exclusively for vehicles licensed in that State. It allows discrimination against interstate transactions. If broadly applied, this decision could balkanize the grid. I recommend that Congress en-

sure that there is no discrimination against interstate users of the grid. Chairman Hoecker has suggested language in his testimony to fix this problem which I heartily endorse.

In summary, I suggest that any legislative reforms focus on facilitating policy choices that will lead to large and robust competitive markets. Open access rules followed by all grid owners will help. Regional transmission organizations will facilitate large regional markets, and mandatory reliability rules will ensure that power is delivered reliably to consumers.

I thank you for your attention this afternoon, and I would recommend the enactment of H.R. 2944 with the modifications noted in my testimony.

Thank you, Mr. Chairman.

[The prepared statement of Hon. William L. Massey follows:]

PREPARED STATEMENT OF WILLIAM L. MASSEY, COMMISSIONER, FEDERAL ENERGY REGULATORY COMMISSION

Mr. Chairman and Members of the Energy and Power Subcommittee: My name is William L. Massey. I have served as a Commissioner of the Federal Energy Regulatory Commission since 1993. I welcome this opportunity to testify with respect to H.R. 2944, the Electricity and Competition Act of 1999. I congratulate Chairman Barton for introducing this important legislation.

I. INTRODUCTION

At this juncture in the transition to competition initiated by the Energy Policy Act of 1992 and Order No. 888, Congress can take the steps necessary to ensure an open, seamless and highly reliable transmission grid that will in turn facilitate vibrantly competitive power markets.

By making the entire interstate transmission grid, regardless of ownership, subject to open access rules, legislative reform can ensure nondiscriminatory access on a nationwide basis. Congress can ensure grid reliability by authorizing a private reliability standards organization that will promulgate mandatory reliability rules. By requiring all grid owners to form appropriately configured regional transmission organizations (RTOs), legislation can help mitigate residual vertical market power, capture for consumers the operational efficiencies created by grid regionalization, and promote large and robust power markets. By authorizing the Commission to mitigate horizontal market power in wholesale or retail markets that may arise from pockets of generation concentration, Congress can ensure that the price for power is determined by the forces of competition rather than by market manipulation.

Why should Congress act now? Simply stated, legislation is necessary to facilitate the removal of barriers that undercut the economic promise of competition. Market and grid access uncertainties that flow from such barriers can stifle investment in necessary generation and exacerbate price volatility. Residual market power, a patchwork of grid rules, or rules followed merely on a voluntary basis, can smother embryonic competitive markets.

Although the prospect of mandatory grid reliability rules appears to enjoy broad industry support, under current law there is no clear path to achieve this goal. Moreover, roughly one third of interstate grid facilities are by law not subject directly to the Commission's pro-competitive policies and standards prohibiting discrimination.

In addition, existing jurisdictional uncertainties may make it difficult to ensure full industry participation in RTOs. Without full participation, the substantial pro-competitive benefits such institutions can facilitate will be available only on a patchwork basis.

Legislation can resolve these uncertainties that now hamper efforts to facilitate competitive wholesale markets and ensure a reliable national grid. And since all power sold at wholesale is ultimately consumed at retail, it is important to understand that efficient wholesale markets are a necessary predicate to efficient retail markets.

II. COMMENTS ON H.R. 2944

At the outset, let me generally associate myself with the testimony of Chairman Hoecker. He and I appear to be generally of a common mind on appropriate legislative reforms.

H.R. 2944 effectively addresses most of the issues mentioned in my introductory comments. The issues it resolves are complex and challenging ones, and I commend Chairman Barton for placing this bill before the House of Representatives.

Although my testimony will focus primarily on legislative reforms that will facilitate wholesale competition, I would like to note briefly for the record that I support retail competition as well. Although wholesale competition is beneficial for consumers in any event, its full promise will not be achieved in the absence of retail customer choice.

A. One Rule for All Transmitting Utilities (Section 102)

This legislation extends the Commission's authority to the grid facilities of all transmitting utilities, including federally-owned utilities, electric cooperatives and municipal utilities. This provision will ensure the benefits of the Commission's open access rules to the users of these facilities. I support this important provision.

Although state regulators in Texas have done a commendable job promoting competition within Texas, I would not further limit federal jurisdiction over ERCOT facilities. Accordingly, I would not recommend the enactment of the bill's language eliminating the Commission's section 211 jurisdiction over ERCOT.

B. Mandatory Reliability Rules (Section 201)

A strong industry consensus appears to support legislation to facilitate mandatory reliability rules. Such rules would provide a firm grid foundation for competitive markets. Section 201 provides that a private standards organization, composed of a broad and balanced cross-section of industry representatives and other experts, would promulgate mandatory rules subject to federal oversight. The North American Electric Reliability Council (NERC) has impressive expertise in this area, and it is my assumption that it will make the internal organizational structural changes, if any, that are necessary to qualify as the private standards organization envisioned by this bill.

It is my view that enactment of this provision is essential to maintaining grid reliability in a competitive era.

C. Regional Transmission Organizations (Section 103)

I strongly support this section's imperative that all transmitting utilities participate in RTOs, and I highly commend Chairman Barton's foresight in recognizing the value of such institutions and requiring universal participation. There is, however, little justification in my view for delaying mandatory RTO participation until 2003. Utilities are already aware that the Commission through its RTO Notice of Proposed Rulemaking has sent an unmistakable signal that the Commission intends for an RTO to form in every region of the country by December 15, 2001.

I am confident that the Commission would promulgate rules that meet the legislation's goals with respect to independence, scope and configuration, corporate form (for-profit and not-for-profit institutions), operational authority and efficiency. I see no reason for Congress to be prescriptive about such issues, or to provide detailed legislative standards for institutions that may need to evolve over time. I would, therefore, suggest the elimination of detailed legislative provisions describing RTO standards and features.

Given the legislation's mandate for RTO participation, I do not understand its rationale for financial incentives for utilities to form RTOs. The need to comply with federal law should be incentive enough, and joining bonuses would appear to be unnecessary. In addition, they are not free, and are paid for by grid users in the form of higher rates. I do, however, support incentives for good performance, measured by reliability, sound congestion management, solid plans for necessary grid expansion, customer satisfaction and similar standards. Well designed performance-based rate incentives would be good public policy.

With regard to determining appropriate RTO scope and configuration, I would prefer that the legislation rely upon the Commission's expertise to determine and apply appropriate factors. If, however, factors are to be specified in legislation, I would add a provision allowing the Commission to apply "any other factor that the Commission determines will promote competitive bulk power markets, reliability and efficiency."

Moreover, I am assuming that transmission owners must join an RTO of appropriate scope and configuration, as determined by the Commission, in order to be in compliance with the legislation. Thus, I do not fully understand the legislative ad-

monition that the Commission shall have no authority to point the utility toward a particular RTO. Absent circumstances I cannot envision, if a utility proposes to participate in an RTO in an inappropriate region (e.g., geographically separate from its operations), the Commission should have the authority to require participation in an appropriate RTO region. I would suggest that the legislation be clarified in this respect.

D. Mergers and Market Power Issues (Section 401)

The amendments to the Commission's authority to review mergers of generation facilities and holding companies are excellent and should be enacted.

For the bulk of mergers that raise no serious market power concerns, the specified deadlines for Commission action would be reasonable. Indeed, the Commission has moved expediently on mergers since issuance of our 1996 Merger Policy Statement. For mergers that do appear to raise market power concerns, however, a hearing before an administrative law judge is sometimes required to resolve factual issues. For such cases, I do not believe that legislative deadlines are appropriate. The Commission is always under pressure to move merger cases through the process as quickly as possible, consistent with thorough review. In such cases, a tight statutory deadline may lead to an ill-considered and hasty approval of an anti-competitive merger, or the unreasonable rejection of a merger that might otherwise be reasonably approved after more thorough review.

Like Chairman Hoecker, I note favorably that both H.R. 1828 and H.R. 2050 would authorize the Commission to examine and address market power in both wholesale and retail markets under certain circumstances. Retail markets will be regional markets that do not respect state boundaries, and it may be difficult for some states to evaluate retail market power in regional markets without federal assistance. Thus, these are important provisions. For robust competitive markets to develop and thrive, any residual market power should be recognized and appropriately mitigated.

E. Discrimination Against Interstate Transactions

Imagine you are driving around I-495, the Washington beltway, and a severe constraint develops due to a traffic accident. Let's assume that the State of Virginia has a policy that favors Virginia motorists. Virginia troopers require all vehicles without Virginia tags to exit immediately so that only Virginia-licensed drivers can travel on the beltway. Maryland applies the same discriminatory policy on the beltway to favor Maryland-licensed motorists. This would impede commerce and would be completely chaotic and unacceptable on interstate highways.

Unfortunately, a recent decision of the 8th Circuit Court of Appeals, *Northern States Power Co., et al. v. FERC,* sanctions this same discriminatory scenario on the interstate electron highway. The court sanctions a preference for in-state uses of the interstate grid. During a constraint, wholesale transactions can be cut so that the local utility can favor its own in-state customers.

Power markets are regional, and do not respect state boundaries. A state-by-state balkanization of the interstate grid would be chaotic and unworkable, just like the hypothetical scenario on the beltway.

Congress should clarify the Federal Power Act to guarantee that all grid users are subject to the same rules, and cannot be bumped off the interstate electron highway by an in-state preference. Chairman Hoecker has suggested clarifying legislative language, which I heartily endorse, in his written testimony.

F. Miscellaneous Issues

Let me in closing comment briefly on three other issues addressed by H.R. 2944:

- I agree with the thrust of the provisions promoting renewably energy, and would endorse virtually any approach that does not distort the competitive marketplace. A portfolio approach is also a reasonable concept.
- I agree with H.R. 2944 that PUHCA should be repealed, while strengthening the "books and records" authorities of FERC and state regulators.
- Regional approaches for the siting of transmission wires are an excellent idea, and appear to track the bill's mandate for regional transmission operations.

III. CONCLUSION

I appreciate this opportunity to comment on H.R. 2944, and will be pleased to answer any questions.

Mr. BARTON. Thank you, Commissioner. I am glad we saved you for last. That is a good way to end the FERC testimony, because

I agree with you—we ought to enact H.R. 2944 with modifications, as long as I agree with the modifications.

We are going to recognize Mr. Burr of North Carolina first, because he has a pending engagement at 2:30, for 5 minutes for questions.

Mr. BURR. Thank you, Mr. Chairman, and it is with our Governor as it relates to the disaster in North Carolina, so I appreciate the chairman's indulgence.

I wish I could say that this panel is different than any that we have had before on electricity deregulation, but it is not. There are differing opinions, differing views, and the reality is that we can't all be right. Somebody is right, somebody is wrong, and it is somewhere in between or maybe that is where the process is supposed to send us.

Commissioner Bailey, let me ask you, your supportive of the 240-day merger language. Let me ask you, if we were to modify the bill to say at the end of 240 days the lack of any FERC decision then automatically approved the merger, would you still be supportive of that language?

Ms. BAILEY. The lack of a decision by FERC would automatically accrue——

Mr. BURR. Approve.

Ms. BAILEY. Approve.

Mr. BURR. Because the current language says at the end of 240 days if FERC has done nothing, the merger is denied. How about if we say the merger is approved?

Ms. BAILEY. Well, I think either case is a little difficult to agree with. I wouldn't dispense with the role as far as FERC is concerned in our merger analysis. My issue is just that it takes entirely too long, whether the issue—whether the merger is approved or disapproved.

To actually say—I have never said that I was in favor of such a decisionmaking process where anything would be automatic. I think that is very difficult to do with these kinds of cases. So, I guess I would say I would probably not be in favor of such a remedy other than to say that I think whatever duration this Congress would put on FERC, I think they would be willing to follow and willing to do, and the resulting decision will be what it will be.

Mr. BURR. Let me ask Commissioner Bailey, because I think you asked specifically that there be flexibility at the end of that 240 days for the tough cases—excuse me, I am sorry, Breathitt. I apologize, Commissioner. Let me ask you, how many mergers has FERC approved in 240 days?

Ms. BREATHITT. At the last Commission meeting, Commissioner Massey actually announced the tally. We have had 30 mergers—isn't it, Bill—since we have—in the last—well, since we have had——

Mr. MASSEY. For mergers that have been filed since the 1996 merger policy statement, 22 out of 25 have been processed within roughly 150 days. The 3 that were not processed within 150 days were set for hearing and have taken longer than that. But that is 88 percent that have been processed within 150 days.

Ms. BREATHITT. So, the few that, since I have been at the Commission, which is 2 years, we have only set several for hearing, and

those are the instances that I said in my testimony, I would ask the committee to amend their language to give us that extra time that we would need for those mergers that we felt presented specific facts, material facts that required extra time for ús to consider.

Mr. BURR. So, with the exception of Commissioner Hebert, 240 days to make a decision is acceptable to you.

Ms. BREATHITT. Yes, I think that is doable.

Mr. BURR. I would tell you that the financial markets work on a much smaller timeframe, and that it is the unpredictableness of 240 days which goes to the heart of what you said one of the objectives that FERC oversight should be to stimulate the development and use of technology. If I understood you correctly, Commissioner Bailey, you said that oversight was needed to stimulate the development and use of technology. Am I correct?

Ms. BAILEY. I made reference to technology from the standpoint of trying to hold back from locking in a 1999 vintage vision because of technological and other advances.

Mr. BURR. Let me just ask all of you to comment, and that will be my last question, Mr. Chairman. How does current FERC oversight stimulate the development of and the use of technology in the marketplace?

Mr. HOECKER. Well, Congressman, I would offer this answer. I think that competition will stimulate technology. I think competition is what we are all after, and I think, to the extent that distributed generation or fuel cell technology, microturbines, or other kinds of gas-based technologies for electric generation want to come into the market, they need to be supplied with markets.

How do they get to those markets? They get there through open access transmission, and without that, without access to markets, those technologies are not going to be as economically supportable——

Mr. BURR. So, in an open marketplace, in retail competition, that does not stimulate the use of new technology? Only FERC can stimulate the use of new technology? Only FERC oversight?

Mr. HOECKER. No, I don't think that is what I said. I said our goal was promoting competition. It is competition. It is the market. And I think you and I agree on this, that it is the market that will stimulate technological developments.

Mr. BURR. And the last comment, Mr. Chairman. Everybody has mentioned reliability, and I think that that is at the heart of every member of this committee. I would ask you, is there a greater degree of reliability with more competition or less competition?

Mr. HOECKER. Congressman, my answer would be competition means a greater degree, and we have had that experience on the gas side with open access to gas, interstate gas transportation. We have a much higher level of reliability, and I expect similar developments on the electric side, as well.

Mr. BARTON. Gentleman's time has expired.

The gentleman from Texas, Mr. Hall, is recognized for 5 minutes.

Mr. HALL. Thank you, Mr. Chairman.

Chairman Massey, I agree with you in saying that you have support for this bill with several amendments, and there is little I could add in the paper. I watch the ads in the paper for cars that

are for sale, particularly antique cars, but I am always concerned when they say, ''1958 Buick, restorable.''

Mr. MASSEY. I am too, Mr. Hall.

Mr. HALL. We can restore it if they give us enough money and a good enough body, right?

Mr. MASSEY. Right.

Mr. HALL. And the chairman's been generous with his time on that. So, let me—Mr. Chairman, you note in your testimony about transmission pricing incentives; that the Commission has asked for comments on the RTO rulemaking on incentives, and starting with you, Mr. Chairman, give me just a snapshot view of where you are in your thinking on this issue.

Mr. HOECKER. Our proposal in the RTO rulemaking is to explore various kinds of incentives that will stimulate more efficient economic behavior by utility transmission owners in the context of RTOs. We mention performance-based rates, congestion pricing, various kinds of things like risk-adjusted rates of returns, things that would encourage better use of transmission and make utilities more willing to access the capital markets to expand the grid where necessary and so forth.

We are in the process of analyzing our comments now, and I expect to have a protracted conversation with my colleagues about where we go from here on that issue, but it is an important one.

Mr. HALL. Ms. Bailey, on pages 8 and 9 of your testimony, you seem to disagree with the chairman on the need for a deadline of the utilities to join an RTO, and you say you believe utilities need the time and flexibility to innovate. If you have a different vision, and apparently you do, from the chairman, of what a restructured bulk power market should look like or just a different way of getting there, which is it? Or is it both?

Ms. BAILEY. My disagreement with the chairman may be just in how to get there. I agree with him wholeheartedly as to the efforts that this Commission has put forward to move toward a competitive bulk power market. To the extent that you have mentioned the mandate issue, I just believe that there is the ability to have more flexibility and innovation as a result of technology and ideas, how that might advance things as opposed to being prescriptive and making a generic timeframe.

Mr. HALL. Mr. Hebert, do you want to add to that or you have any different view? I would be surprised if you didn't.

Mr. HEBERT. Congressman Hall, I do, and I appreciate you giving me the opportunity to answer it.

I think it is ultimately important that we provide incentives, whether it be accelerated depreciation, increased rates of return based on risk, acquisition adjustment, or other incentives, quite frankly, that we haven't even thought of at this point. And it does go back to Congressman Burr's question to a certain degree, too, because he was asking about technology and how do we provide for technological advances?

Well, we do that through competition, but he had a very good question in asking whether or not FERC can provide it. Well, no, sir; FERC cannot provide it. Competition can provide it. I know someone earlier was looking for a definition of competition, which is where supply and demand can meet, but when they start to meet

that is exactly when you get the investment necessary to try create technological advances much like we have seen after the Green decision in telecommunications. But FERC has to take the initiative and provide the economic incentive to do so.

Mr. HALL. You used the, I think, your view of separate transmission business on page 4 of your testimony, and when you use the FTC's word, quote a "clean break," unquote, do you mean the total separation of transmission from generation, including ownership and control?

Mr. HEBERT. Yes, sir; that is what it means.

Mr. HALL. Full go.

Mr. HEBERT. Absolutely. That would make it truly independent.

Mr. HALL. And on page 5, is it your view that FERC should no longer review mergers?

Mr. HEBERT. Yes, sir; it is.

Mr. HALL. Time limitation on FERC mergers—I think the gentleman from North Carolina got into that—resolve any of your concerns?

Mr. HEBERT. It does in the sense that I think it is better than what we currently have, although I will have to step back one moment and commend the Chair and the Commission for doing a good job here in the recent past on mergers.

My point is this though: Utilities are not exempt. They have no immunity from antitrust laws, and I have yet to be convinced by anyone that there is anything in market power concerns that they can't be taken care of otherwise, through the DOJ or the FTC, or under the Public Utility Holding Company Act and the SEC. So, my point is, why duplicate this service if indeed it is not necessary? We are not an antitrust agency, but we do have some in the United States.

Mr. HALL. I think my time is up or I would ask the chairman if he would like to answer that.

Mr. Chairman, would you like to make comment on Mr. Hebert's——

Mr. HOECKER. Well, I of course appreciate——

Mr. HALL. I thought he was pretty generous in acknowledging that in some things you had done a good job.

Mr. HOECKER. Well, I think that is one for our side, but I am——

Mr. HALL. It still 3 to 2, isn't it?

Go ahead.

Mr. HOECKER. That is the story, isn't it?

I am very anxious that this Commission continue to process merger applications responsibly and quickly to the maximum extent we can. We have lived up to our promise to the public in our policy statement 3 years ago, but I do think that whereas the antitrust agencies look periodically at the electricity market, the bulk power markets, and the consequences of mergers for competition, we do it systematically.

We are experts in that area. We understand how those industries and those companies work, and we think we are much more capable of conditioning mergers in a way that will allow them to go forward with some fine-tuning rather than the kind of more dramatic antitrust type solutions that you get from antitrust agencies.

And I would add that I take exception to Commissioner Hebert's characterization. It is very clear in our case law that we are responsible for looking after antitrust type concerns in the context of our regulation.

Mr. HALL. Thank you, Mr. Chairman.

Mr. BARTON. Thank you.

The gentleman from Florida, Mr. Bilirakis, is recognized for 5 minutes.

Mr. BILIRAKIS. Thank you, Mr. Chairman.

I wasn't here for an opening statement, and I would just merely add to all of the others that may have been commending and congratulating the chairman to the effect that he has been just about as fair as anybody could possibly be up here and always open-minded and listen to all of us. There are some areas that have not been satisfactorily as far as some of us are concerned, but it hasn't been because he had closed mind to those ideas.

One of the areas that greatly concerns me, and I am just not clear on, is section 102, the open access for all transmitting utilities. It seems that under those provisions FERC will be able to order electricity be delivered to retail customers even if a State has not elected to have retail competition.

We worked awfully hard on the date certain idea and we thought we had that issue resolved, and then this language pops up. So, I guess I would ask all of you your opinion. Should I, from my view point or from the view point of those who are concerned, been concerned about the date certain concept and open access? Should I be concerned? Do you feel that that provision gives FERC the authority, to order retail competition in closed States? Mr. Chairman?

Mr. HOECKER. Congressman Bilirakis, I don't think that that provision is designed to do that. I view 102 as an endorsement of the Commission's initiative in Order 888, which requires open access to bulk power facilities, i.e., high voltage transmission. Sometimes high voltage transmission is delivered directly off the grid to what would arguably be a retail-type customer. Order 888 is very clear that we would presume a distribution function in those instances so that States would maintain jurisdiction and be able to do such things as recover retail transition costs.

So, I think that it is clear, and it is certainly our intention, and it is the way I read the bill, that we leave regulation of the distribution function and access to the retail markets to the States.

Mr. BILIRAKIS. Well, but subparagraph 2, notwithstanding paragraph 1, "The Commission may issue an order that requires the transmission of electric energy directly or indirectly to retail electric consumers who are served by local distribution facilities that are subject to open access." And I will admit I am not quite clear on those last three or four words. I mean, it seems to be pretty direct.

Mr. HOECKER. If the transaction is going directly to a retail customer, we can ensure that the transmission is available to complete that transaction.

Mr. BARTON. Would the chairman yield?

Mr. HOECKER. Yes, sir.

Mr. BARTON. If Mr. Largent can answer a question for the Deputy Secretary, I think I can answer a question for the Chairman

of the FERC Commission. The key phrase there is "subject to open access." So, in a closed State, you are not subject to open access, and that is the key phrase. So, to pick a State out of the air—Florida—which is not subject to open access at the State level, FERC would not have jurisdiction, if that eases the gentleman's mind.

Mr. BILIRAKIS. Well, it would ease it I think if we took another look at the language and change it in such a way so that this concern is addressed.

And if FERC orders the utility to expand its transmission capabilities, who should pay for that expansion, Mr. Chairman?

Mr. HOECKER. Well, that is a good question.

Mr. BILIRAKIS. I gather the previous one was not.

Mr. HOECKER. Your questions just keep getting better.

The bill provides for authority for the Commission to order expansions subject to State siting authority. I believe I said in my written testimony we didn't believe, or I didn't believe, that that was necessary for us to have. But if the grid is expanded, usually the ratepayers or the wholesale customers in the locale of—in the service territory of—the utility that is either expanding or in whose territory the expansion occurs will pick up the tab, which is a problem if the expansion is made for the benefit of ratepayers in another jurisdiction or another service territory.

So, you raise a very, very difficult question. And it is one reason why we think that regional institutions, like RTOs, where utilities can work these kinds of problems out and allocate those costs on an equitable basis is very important.

Mr. BILIRAKIS. Well, I guess my time is up. It amazing that 5 minutes went that quickly, but that is what it is.

All right. Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Chairman Bilirakis.

Recognize the gentleman from Ohio, Mr. Sawyer.

Mr. SAWYER. Thank you, Mr. Chairman.

I am struck by the last comment in light of the final question that I asked before we broke for lunch. I remember the Deputy Secretary, when I asked him about siting decisions, suggesting that we could get all the States together and they could sort of work it out. That was my reaction too. I was tempted to ask him if that would work sort of like the multi-State, low-level, nuclear waste compact, but I didn't have the heart to do it.

How do you envision resolving precisely the kind of siting difficulties that clearly are a part of this business? You have authority in terms of natural gas; that is difficult enough. Do you see the need for similar kinds of authority with regard to electric transmission?

Mr. HOECKER. Well, I believe the Secretary's response was that there wasn't a history of Federal siting authority on the electric side, and I think that one could certainly make an argument that in a competitive market, where the interstate traffic and electrons are so much more important than they used to be, that some regional or Federal authority to site transmission might be very helpful.

Rather than recommend that, however, I have put my eggs in the RTO basket or in some equivalent regional organization or compact that will be able to bring together the people with the

most identifiable and likely common needs in a region in terms of getting to loads, getting generation to market, and let them decide what the appropriate expansion of the system is.

Mr. SAWYER. Are there other comments from other commissioners?

Ms. BREATHITT. I will add from my prior experience as a State commissioner that siting is held near and dear to the hearts of State commissions. If we did it at FERC, it would require changing the Federal Power Act, and I agree with the chairman that I am not advocating doing that.

You will probably hear from the next panel, from NARUC, how they feel about siting, and I know that some have called for a comparable siting authority with respect to electricity that we have in gas, but I think regional consultation with RTOs, with State commissions in the region where the power lines may need to go through, could be an answer to facilitate expansion.

Mr. SAWYER. Let me ask another question. When we talk—the chairman used the term expansion with the service territory of the utility making the expansion. In a competitive environment what do we mean by "service territory?"

Mr. HOECKER. That is a good question—I am sorry. In a classic sense, of course, a service territory is——

Mr. SAWYER. I know what it was. I am trying to figure out what it is going to be and how some of these old structures that worked well in a rate of return, obligation to serve environment will work in a competitive market.

Mr. HOECKER. There will continue to be utilities who are load-serving entities who have distribution and are obligated by State or local law to serve all the customers in that area.

Mr. SAWYER. So, you are talking about a distribution definition.

Mr. HOECKER. Right. At the bulk power level, you are absolutely right. You have merchant generators who can sell anywhere in the marketplace under whatever contracts they can get, and that does tend to change the concept of a service territory.

Mr. SAWYER. Let me ask one more question. Well, I will tell you what, I will wait for a second round. We are starting to——

Mr. BILIRAKIS [presiding]. I don't know whether there is going to be a second round or not; it is up to the chairman. So, without objection, you are recognized for an additional minute.

Mr. SAWYER. We have talked a great deal about the formation of RTOs and the mandate that appears to depart from the where the NOPR was heading. I am concerned about once formed are they presumed to serve a useful purpose in the same configuration for all time or are there—do you anticipate vehicles for shifting the design, and if that is the case, why not allow a much more voluntary formation than the one that I have heard several people talk about here today? How do you envision that changing?

Mr. MASSEY. Well, my view is we need to get them up and going in every region of the country, and our policy provides that they should not build in any features that would prohibit their evolution over time. They may very well evolve. They may change shape; they may get larger; they may move from an ISO structure to a transco structure, and it is the Commission's official policy that the

RTO itself not build into its structure any features that would inhibit its evolution to a more efficient structure over time.

Mr. BILIRAKIS. Very, very briefly, please, Tom.

Mr. SAWYER. I will pause, thank you.

Mr. BILIRAKIS. All right, good. Thank you.

Mr. Rogan.

Mr. ROGAN. Mr. Chairman, I do have a couple of questions, but I am pleased to yield to my friend from Ohio for a follow-up.

Mr. SAWYER. I appreciate the gentleman's generosity, but I wanted to pose a question. I don't think we are going to get a much more involved answer at this point, but I think it is a question that deserves an answer as we move in building consensus legislation. So, I thank the gentleman.

Mr. ROGAN. Thank you, Mr. Chairman, and, Mr. Chairman, I also echo your comments earlier and wish to associate myself with them in commending Chairman Barton for the yeoman's work that he has put into this particular effort. I welcome all of the witnesses.

I would like to get the opinion of each of the commissioners as to how we should—or how you anticipate FERC would deal with transmission over non-interstate commerce lines; in other words, non-contiguous States? Maybe I can just start at the end.

Ms. BAILEY. When you say non-contiguous, how FERC would deal with transmission?

Mr. ROGAN. Yes.

Ms. BAILEY. That is the crux of our open access; our Order 888 is open access. I am not quite sure where your question is——

Mr. ROGAN. Well, I am really asking, under the terms of this bill, if this bill were to become law, how would FERC, in your opinion, deal with regulating transmission that would be not over interstate commerce, traditional interstate commerce?

Ms. BAILEY. To the extent you are talking about PMAs or TVA, BPA, those kinds of entities——

Mr. ROGAN. Yes.

Ms. BAILEY. [continuing] that we have not—okay. I previously probably have not taken a stand myself on that position, but to the extent that we are trying to move toward what you would call superhighway in electricity, I think there I would have to say, yes, they need to be brought into the fold.

So, to the extent that I am sure you have probably already been in discussions, and this bill is probably a consensus, and these entities are aware, I am supportive of what you have in there. So, I think to the extent that we want to avoid the swiss cheese factor and the patchwork of access, I think it is key that we probably move in this direction.

Ms. BREATHITT. I had mentioned earlier that a lot of the non-jurisdictional entities, such as the Federal PMAs and coops, that transmit electricity have filed reciprocity, open access tariffs with us, but I agree with my colleague, Commissioner Bailey, that to have what we call, when we talk about a seamless grid, that 30 percent of the—roughly the 30 percent of transmission that is not included in our tariffs eventually should be and probably sooner rather than later.

Mr. ROGAN. Mr. Chairman?

Mr. HOECKER. Congressman, I think my colleagues have hit the nail on the head. The nubs of it, I think, are that it is hard to imagine transmission that isn't in interstate commerce. There is a lot of transmission that isn't jurisdictional to the FERC for legal reasons, but almost all of it is part of an integrated grid over which electrons flow in and out of States, in and out of power marketing agencies, in and out of municipal systems, and what we are suggesting is that we provide a uniform standard of comparable service and access to all that transmission, and without exception, and that is the way we will get to a workable market.

Mr. ROGAN. Thank you.

Mr. HEBERT. Thank you, Congressman Rogan. When I take the approach looking at BPA and TVA, I take a little different thought process and try to come up with a business solution, and it is my thought that we can resolve it without having additional jurisdiction coming to FERC, and that would be to get them to sell of their transmission assets to a jurisdictional utility, and therefore we would—it would accomplish the same end but through a different means. So, that would be my preference, and I have made that clear.

I know you, as a former State legislator, understand when it comes to munis that you have got other tax issues of local and State concern that come up.

Mr. ROGAN. Thank you.

Mr. MASSEY. My thinking, Congressman, is that they would be just like the interstate grid, interstate transmission, and would be subject to the provisions of Order 888, which requires open access service, unless the Congress specifies a different way for us to regulate those systems.

The idea is creating the largest markets possible all across the country, and that is a function regulators of interstate commerce, which is what we are, can facilitate. A State can open its borders to competition, but it is very hard for that single State to ensure grid access in the surrounding States. Only federal regulators can do that and eliminate any swiss cheese effects.

Mr. ROGAN. Mr. Chairman, thank you. I yield back.

Mr. BARTON I thank the gentleman from California.

We recognize the gentlelady from Missouri for 5 minutes for questions.

Ms. MCCARTHY. Thank you very much, Mr. Chairman.

I wanted to ask some clarification on how the regional transmission organizations that utilities join work with the transmission agencies that States join. Are they the same? Because if a utility regional—utilities join a former regional transmission organization, is it States that have to belong to that? I am a little confused.

My only other experience with interstate compacts was with the idea that Congress had at one point in time that if the States decided where to send the level nuclear waste, that would be the best solution, and it didn't work. So, could one of you clarify for me from the bill how these would work, these regional transmission siting agencies that States join, and then the regional transmission organizations that the utilities join?

Mr. HOECKER. Regional transmission organizations are either——

Ms. MCCARTHY. Well, let me make it clear. What if Missouri joins with New York, and that becomes our regional transmission siting agency, but our utilities in our two States don't join with those parties. The New York utilities join with Connecticut, and the Missouri utilities join with Texas? Well, who is talking to whom, and how does this all work?

Mr. HOECKER. Okay. Our proposed rule would have contiguous utilities joining together in a regional transmitting grid.

Ms. MCCARTHY. Oh, so you are going to do this by rule.

Mr. HOECKER. Well, we are proposing to urge utilities to do it voluntarily, but we have set some baseline criteria for how these organizations ought to work and when they should begin to form.

Ms. MCCARTHY. So, why do we need two different ones then, if you are going to tell the utilities to join in these contiguous States an the States to join in these contiguous States? Are we not—are we really opening competition? I guess that is where I am coming to.

Mr. HOECKER. That is a good question. There are I think four or five States now—Wisconsin, maybe Illinois, a couple of other States—that have actually told their utilities to join a FERC-authorized regional transmission organization. Transmission is regulated at the Federal level. What we are trying to do is to create a broad market at the bulk power level, which is basically high-voltage transmission and energy sales and purchases between utility companies. And that will create access at the wholesale level that will facilitate what the States do at the retail level.

Ms. MCCARTHY. Is it fair to presume that you, in a sense, will control competition, then, by the way you design these things?

Mr. HOECKER. Well, we are asking the utilities to design it. We are finding in many States, including California, and the States within PJM and NEPOOL, which have now got an RTO, that State regulators have been very influential in how these organizations are governed, what their policies are, how the wholesale transmission entity interacts with competition at the retail level.

So, this is really an opportunity, as I view it, for regions and for States to put their imprint on the bulk power market in a way that they can't now. They can engage in—help engage in regional planning activities for expansion of the transmission grid that we were talking about earlier, enhancing reliability measures, ensuring that——

Ms. MCCARTHY. So, let me ask a question. So, my Missouri utilities will, based on your rule, likely join with other utilities right in the Midwest region. You are going to——

Mr. HOECKER. In some logical, economic, and physical marketplace, yes.

Ms. MCCARTHY. So, you will control that competition there——

Mr. HOECKER. I don't think——

Ms. MCCARTHY. [continuing] and that will——

Mr. HOECKER. I am sorry. I didn't mean to interrupt.

Ms. MCCARTHY. But what if they wanted to join with Texas or somebody else? I mean, that is not contiguous nor logically in the region, but it might make good economic sense.

Mr. HOECKER. Well, it would have to be a contiguous marketplace.

Ms. MCCARTHY. I am sorry?

Mr. HOECKER. One of the propositions in our proposed rule—and of course we are still taking comment on this and evaluating that—is a regional scope and configuration that for an RTO to operate appropriately and to be acceptable, it should replicate in some sense a historical, physical, and commercial marketplace that already exists—utilities that do transactions with each other. If Missouri finds itself in a position of sharing a common interest in terms of utility commerce with Texas, it need only make that argument to us, and we will decide whether in fact that is the case.

Ms. MCCARTHY. Yes, and that is my point—you will control competition. I happen to think, though, by the way, with Missouri being a low-cost State, that just staying in the Midwest and making sure we all work together, which seems to be working well now, will continue. It ain't broke out there. We don't need to fix it. But I am just wondering who is in charge here.

And, Mr. Chairman, thank you for indulging me with these questions.

Mr. BARTON. Thank you, Chairwoman—I mean, Congresswoman.

Mr. Pickering is recognized for 5 minutes.

Mr. PICKERING. Thank you, Mr. Chairman.

Let me ask just a quick question of each of you first to put things in context, and I am just going to ask a question, do you support or oppose an incentive-based RTO approach or a mandatory RTO approach? And, so if we could start with Commissioner Bailey, do you support mandatory RTO or an incentive-based approach?

Ms. BAILEY. Incentive-based, to use your words, incentive-based.

Mr. PICKERING. Ms. Breathitt—if that is the correct way to pronounce it?

Ms. BREATHITT. My opening statement reflected that I think a voluntary approach is the best course to be on at this time.

Mr. PICKERING. Chairman?

Mr. HOECKER. I believe in supporting incentives in the right context. If your question is should incentives be the only mechanism for creating these institutions, I would have to say no.

Mr. PICKERING. So, you would support a combination of a mandatory stick at the end as well as incentive-based approach.

Mr. HOECKER. Well, even voluntary. I think that a lot of utilities find competition to be in their interest.

Mr. PICKERING. So, you—are you saying that there is a way to structure a voluntary, incentive-based approach without a mandatory approach?

Mr. HOECKER. Well, that is what we have proposed. I don't know if I would call it incentive-based éntirely, but there are certainly incentivés that we are going to seriously consider.

Mr. PICKERING. Commissioner Hebert?

Mr. HEBERT. Incentive-based or voluntary. I am not sure if you are using those synonymously. I know Commissioner Breathitt had said voluntary. So, I guess to specific I would say incentive-based.

Mr. PICKERING. Commissioner Massey?

Mr. MASSEY. I support incentives for good performance once the RTOs are formed. Performance-based rate incentives sound like a good idea to me. The customers get good performance that way.

With respect to joining bonuses, I am not in favor of joining bonuses. I do believe——

Mr. PICKERING. How would you define a joining bonus?

Mr. MASSEY. I would define it as giving some sort of a financial sweetener to a utility to entice them to join an RTO. My concern is that someone has to pay for those, and it is the customers of the utility through higher rates, and if we can achieve the formation of RTOs without increasing rates in that way, that would be my preference. But once they are formed, I do believe that we should find ways, through performance-based rates, to incent good performance.

Mr. PICKERING. Let me clarify in one additional way. If you don't believe in bonuses, do you believe in sanctions or penalties if they don't form RTOs or mandates to force formation of an RTO of a specific size or specific criteria?

Mr. MASSEY. I would like to see RTOs form in every region of the country, and——

Mr. PICKERING. Does that mean FERC should have the authority to mandate that?

Mr. MASSEY. Well, the Commission has market-based rate authority, for example, which might be——

Mr. PICKERING. So, just a clean, clear answer yes or no. Do you support a FERC authority to mandate RTOs?

Mr. MASSEY. Yes, I do.

Mr. PICKERING. Okay. So, 4 to 1, is that correct? Incentive voluntary approach versus a mandated approach?

Mr. HOECKER. Well, let me clear about this.

Mr. PICKERING. Maybe 3 to 2.

Mr. HOECKER. I think we are going to explore with the industry ways to get our desired goals through a voluntary approach, but that the Commission may find it necessary in some instances in the future to explore other kinds of approaches.

If, for example, Congressman, all the utilities in your part of the country were to join an RTO and began to enjoy the benefits of that regional marketplace, but one or two utilities with key transmission facilities refused to join or refused to fill in the blank spots, the Commission is confronted with a tough policy choice there.

Mr. PICKERING. Okay. Let me now go into the details or the substantive if you were to take an incentive-based approach. Now, the chairman, Chairman Barton, has included some incentives that were included in a bill by Mr. Sawyer that would give incentives to form the RTOs or the transmission organizations. Do you support those provisions, and what in addition should be included in legislation to give the greatest opportunity for a voluntary, incentive-based approach to work?

Let me start, first, with Commissioner Hebert, and then, Chairman, if you want to add anything and anybody else on the panel.

Mr. HEBERT. Thank you, Congressman Pickering. I have supported incentives, as you know, and I have had a conversation, as well, with Congressman Sawyer, and he knows that I do support that and think that is exactly the direction that this Commission should move in.

If we do it voluntarily, not only do we save ourself the time in not having to get out and mandate these, we also save our time,

because through the incentive process, you are not going to have the lawsuits that you would otherwise have through trying to force, such as you have right now with 888 and northern States. It is the better route to take. It is an easier route to take, and with everything being as unclear as it is right now, I see no reason to go in that direction.

But the exact incentives that you are looking for would be something in the neighborhood of accelerated depreciation, an increased return on equity based on risk, an acquisition adjustment. Because in the end, when you are looking at the acquisition of those assets, there are two things that have to be answered. The selling company wants to know how much of it can they keep? In other words, the stockholders want to know how much of it can they keep? My suggestion is that you allow them to keep half of it; the other half would go to the ratepayers. When it comes to the other side, the acquiring company wants to know what type returns they are going to be able to make, and you need to also answer what the valuation will be based on when it comes to their rate of return.

Mr. PICKERING. Chairman?

Mr. HOECKER. I believe 202(h) is the provision you are looking at, and I find the list of potential incentive transmission pricing policies listed there to be pretty attractive, and we are going to be sorting through those and figuring out how we can make that or something similar work.

I would say, however, that the provision appears to provide incentives to transmitting utilities to form RTOs, and I suggest that the bill may be internally inconsistent in the sense that there is a mandate and then this incentive provision. I, frankly, think that utilities are going to want to get in the transmission business or set up a separate transmission company if they think that is going to be a viable and competitive and economically sound line of business, and that is what we ought to focus on—inducing good performance, as Commissioner Massey says, but also making it clear that these new companies are going to be able to attract capital in the marketplace, expand the grid where necessary, and that they are not going to be penalized in their rates of return because of the establishment of a transmission company.

Mr. PICKERING. How would you resolve the internal conflict?

Mr. BILIRAKIS [presiding]. We are running out of time here, Chip.

Mr. PICKERING. I yield back.

Mr. BILIRAKIS. I would hope that what they are telling us is that the bill's language should be changed in that regard, and I suppose that is where you were.

Mr. PICKERING. Yes, they were going in the right direction. Thank you, Mr. Chairman.

Mr. BILIRAKIS. Mr. Largent to inquire.

Mr. LARGENT. Thank you, Mr. Chairman.

Mr. Hoecker, does the FERC currently have the authority to address market power in the wholesale markets?

Mr. HOECKER. We have authority to address market power most specifically when we review mergers, when we set rates and terms and conditions of service. I think that our market power review is inherent in the Federal Power Act, but that there are, I think, some limitations in terms of the kinds of remedies we can achieve

and how we can address market power concerns in a more competitive environment when utilities are required to change their conduct and not to, for example, operate their transmission to favor their own generation.

Mr. LARGENT. Is the wholesale market not competitive today? Is that what you are saying?

Mr. HOECKER. I don't think it is entirely competitive, no.

Mr. LARGENT. And why not?

Mr. HOECKER. Well, I think it is—I think, first of all, there are big parts of the wholesale market that are not subject to open access or part of the interstate——

Mr. LARGENT. Like TVA or munis or——

Mr. HOECKER. Yes, I think that is certainly a big question as to how we could possibly assure against the exercise of market power in those instances.

Mr. LARGENT. What about in areas that FERC does have authority over the transmission with IOUs? Have you, at the FERC, have you guys looked at cases where you believe market power has existed, but you felt like that your remedies have fallen short?

Mr. HOECKER. Well, RTOs maybe, you can view that as one example. The fact is that utility companies have come through this century as largely vertically integrated companies with transmission distribution and generation and that will, quite understandably, work in the market in ways that will favor the biggest return on all those assets together.

RTOs are one way of separating or functionally disaggregating parts of the industry so that there is more competition, there is more confidence in the impartiality, shall we say, of the operation of the transmission system. Without remedies like that separation and I very seldom bring up the "D" word, because it is kind of a red flag, but without those kinds of remedies, we have to resort to things like cost of service ratemaking and to treat utility companies as if we were in the 1960's instead of on the verge of a new millennium and a market economy for energy.

Mr. LARGENT. Well speaking of that, have you guys ever had to do that? In other words, revoke somebody's market-based rates as a penalty for exerting market power?

Mr. HOECKER. Well, we have granted market-based rates in hundreds of instances, but we have said, for example, that in certain geographic areas or certain markets where competition cannot be shown in the generation area, we would not grant market-based rates.

Mr. LARGENT. You have done—you have denied——

Mr. HOECKER. We have done that, yes.

Mr. LARGENT. Okay. Let me ask you another question, and that is that different regulatory schemes found within Mr. Barton's bill on transmission, on bundled versus unbundled sales. Is that workable? I mean, how can you do that?

Mr. HOECKER. Are you talking about section 101?

Mr. LARGENT. What section is that?

Mr. HOECKER. The jurisdictional provision.

Mr. LARGENT. I think it is section 101.

Mr. HOECKER. Yes.

Mr. LARGENT. Where you have a State PUC regulating transmission for bundled sales and FERC regulating transmission of unbundled sales, and how do you do that on a national grid? I mean, is that workable?

Mr. HOECKER. It is difficult. I think that the Federal Power Act speaks to our jurisdiction over transmission and says very little else. But over the years, we have accommodated the States, and they have generally regulated the rates, terms and conditions of service or transmission that is bundled in a retail transaction. And I think that that is an effort to strike a balance over the use of facilities that we share jurisdiction over arguably. And that works okay if we can all agree.

Mention was made earlier and in my testimony about the 8th Circuit decision that would allow States to, rather than curtail their own native load or their own retail markets, to prefer those and to curtail somebody else, and that is on the transmission level. That decision is somewhat problematic, because in Order 888 we said that all uses of the transmission should be comparable; that is, if a utility finds itself constrained in terms of transmission and has to curtail, it should do that pro rata across all uses of that transmission. This court decision appears to say that that is an interference with the retail marketplace even though we are talking about transmission.

It is a very confusing area, and if that decision were applied very broadly, I think there is a substantial risk of some serious balkanization of the wholesale marketplace. And, quite frankly, I think a competitive marketplace where everyone gets the same treatment in terms of use of the wires, is the best protection that State retail customers and State commissions have, and I hope we can persuade them of that.

Mr. LARGENT. Mr. Chairman, I see my time is up. I want to take advantage of this excellent panel and hopefully get a chance on a second round of questioning.

Mr. BILIRAKIS. Well, that is really up to Mr. Barton. I do know that the next panel has been sitting very patiently since 10 o'clock this morning, but that is up to the chairman and whatever he should decide to do.

Mr.—he has gone to Norfolk?

Mr. Markey to inquire.

Mr. MARKEY. Thank you, Mr. Chairman. Thank you very much.

Mr. BILIRAKIS. Your time started a few seconds ago.

Mr. MARKEY. Thank you, Mr. Chairman.

Welcome, sir. I would like to examine the Barton bill and have you look at section 101 and ask whether or not you believe that that section codifies the recent 8th Circuit decision and, if so, what impact that would have on FERC's ability to prevent utility monopolies to grant themselves preferential service for their own use and prevent competitors from fairly, effectively, and efficiently utilizing the transmission grid?

Mr. HOECKER. Well, arguably, you can certainly read the 8th Circuit decision as doing just that. Whether this language—I think this language basically codifies what we said in Order 888, which is that to the extent transmission is bundled within a retail service, to that extent, we would defer to the States in terms of the regula-

tion of rates and terms and conditions of service, provided—and this is a big provided—provided that all uses of the transmission system are comparable and that a utility applies its curtailment policies, for example, on a prorated basis to the all the uses. The 8th Circuit departs from that formulation, but I don't necessarily see this language adopting that.

Mr. MARKEY. You don't—so you don't—in your view, section 101 does not undermine the Commission's comparability standard?

Mr. HOECKER. I don't think it has to, and I think that the Commission——

Mr. MARKEY. You don't think it has to? I mean, is it clear that it does or doesn't or would you need—do you need to be clarified or are you going to leave it for a court decision? Does the 8th Circuit have to go in and clarify? I mean, what do you mean it doesn't necessarily have to?

Mr. HOECKER. Well, I would put it this way: The call here that States have authority over that portion of transmission that is bundled within a retail service was a call that this Commission made in 1996, and if the principles of comparability are adhered to by providers of transmission, I don't think that that necessarily has an adverse effect on our competitive objectives.

If, however, like the 8th Circuit decision, this jurisdictional call is leveraged into the kind of discriminatory practice that you are talking about, that is a problem. I don't necessarily think that this language necessarily gets us to that point, but it certainly lays the predicate for it. I agree with you.

Mr. MARKEY. Okay. Now, the RTO provisions of the Barton bill appear to tell the FERC to accept utility RTO proposals but give FERC no other options. Is that a correct assessment?

Mr. HOECKER. I am very sorry; would you please say that again?

Mr. MARKEY. I said that the RTO provisions in the Barton bill appear to tell FERC to accept utility RTO proposals but give the FERC no other options. Is that your reading of the Barton language?

Mr. HOECKER. Yes, I think that it pretty much says if the utility proposal conforms to the criteria in the statute, that we should accept it.

Mr. MARKEY. Okay. So, under the RTO proposal, can FERC reject an RTO that is too small, not sufficiently independent, or without adequate authority?

Mr. HOECKER. Under the legislation, I think we could. It does refer to scope and configuration, and I am assuming that we would have to be clearer and more detailed in the statute in implementing that provision.

Mr. MARKEY. So, you think you would have sufficient latitude, then, to foster an RTO that satisfies the minimum conditions under the language?

Mr. HOECKER. Yes. The real problem I have is that it is not clear that 2, 3 years hence these are necessarily going to be all the appropriate minimum conditions that might be desirable from a commercial standpoint.

Mr. MARKEY. Okay. So, in you mind, what would be the reason for providing incentives to an RTO that is already in existence?

Mr. HOECKER. I think that the view I have of incentives generally runs to encouraging utilities to engage in the most efficient economic behavior. Certainly, whether or not they are in RTOs, we would want them to do that, but in particular I think that the benefits of RTOs and the benefits of incenting utilities to perform better is worth it to this Commission, and hopefully the Congress, to sweeten the pot a little bit.

Mr. MARKEY. If I am correct, do you establish the FERC——

Mr. BILIRAKIS. The gentleman's time is up. Now, how much further?

Mr. MARKEY. I have one question.

Mr. BILIRAKIS. One question with a very brief answered required.

Mr. MARKEY. If I am correct, the established FERC position is to eliminate rate pancaking. Is the provision on incentive rates or phasing out pancaking at odds with FERC policy?

Mr. BILIRAKIS. Brief response, please.

Mr. HOECKER. I don't think it is.

Mr. MARKEY. You don't think it is.

Thank you, Mr. Chairman.

Mr. BILIRAKIS. Mr. Bryant, who has been waiting very patiently.

Mr. BRYANT. Thank you, Mr. Chairman. I will be brief. I want to yield the balance of my time to my colleague from Oklahoma.

But, Mr. Chairman, I have a question regarding H.R. 2944 and its allowance to TVA to sell wholesale power outside the so-called fence. Could TVA get FERC approval to charge market-based rates for these sales outside the fence? And, if you could, could you answer that for me in writing?

Mr. HOECKER. I would be delighted to do it in writing.

Mr. BRYANT. Okay. And, second, my concern is that we deregulate—we truly deregulate as best we can, realizing there is a need for some regulation. What—could you answer again in writing what you anticipate under a Barton-type bill to be the growth in the size of your organization? I assume you are going to need additional manpower, funds, and so forth. If you could give us somewhat of a reasonable projection based on a Barton-type bill.

Mr. HOECKER. I will do the very best.

Mr. BRYANT. Is that feasible? Okay.

And at this time, I would yield the balance of my time to Mr. Largent.´

Mr. LARGENT. Thank you, my friend from Tennessee.

Mr. Hebert, I wanted to ask you one question about part of your testimony on page—well, what page is it; there is not a number on it. But you said that earlier existing ISOs failed the independence test. Could you comment on that?

Mr. HEBERT. Yes, thank you, Congressman Largent. The ISOs as we know them today, the very genius in the ISO itself is in the name—independent system operator—where they are anything but truly independent, because you have a stakeholder group who is going to make the decision when it comes to planning and forecasting and the organization itself. And to become completely independent my suggestion is that we move toward an independent transmission company that has total separation from operation and control. We have someone who is in the transmission business.

Now, as you know, and you and I have had private conversations, and it is my testimony and my belief that at rates of return of under 10 percent certainly we are not going to get people in the transmission business, so we have got to give pricing signals to get them in the business. Now, the way for us to do that is through the incentive process, and you will have people come to the table. I have people come to my office and speak with me privately. I had a gentleman in my office I was speaking about earlier today who had $50 billion who was ready to put one together. These people are ready to do it, but they are not going to do it for less than 10 percent when on the open market they can make 12 and 15 and 18 every day.

Mr. LARGENT. Well, the current—the ISOs that exist today, do they not have consumer advocate groups that are part of the board or——

Mr. HEBERT. Yes.

Mr. LARGENT. But you are saying that they don't—it is the IOUs or the stakeholders that dominate the board is what you are saying.

Mr. HEBERT. Well, the consumer groups are one of the stakeholders. You also have the companies themselves. You have stakeholder groups which are defined by the ISO themselves.

Mr. LARGENT. But I am talking about consumer advocacy groups that are not stakeholders in transmission or—I mean, there is not consumer groups that are stakeholders in owning generation assets or transmission assets or distribution assets, are there? I mean, you said that consumer groups are stakeholders. In what sense? As ratepayers?

Mr. HEBERT. No, in the sense—let me give you California, for example. You have consumer advocates, which I don't know how many seats they hold currently on the committee, but they hold seats on the committee.

Mr. LARGENT. Right.

Mr. HEBERT. Which is a committee of 25, I believe.

Mr. LARGENT. Well, I guess when I heard you say stakeholders, I assumed you meant that people who were regulating themselves. Consumer groups aren't regulating themselves other than being ratepayers. You see what I am saying? I mean, if a consumer advocacy group is sitting at the table, now there may be an issue about the ratio of IOUs versus consumer groups that throws the balance to what I term stakeholders, and that may be an issue. Maybe that is what you are talking about in terms of losing independence. Is that what you are saying?

Mr. HEBERT. Well, I guess part of the problem you and I are getting into is semantically in that I have become quite confused on exactly what a consumer group is, be it from my days in the State legislature to chairman of the State commission, to here. What is a consumer group to one is certainly just an advocate for an interest to another, as you know. You know that; you deal with on a daily basis.

But the ISOs themselves are not independent to the extent that you don't have total separation from operation and control. The operators are still players in controlling the ISO itself. When it comes

to an independent, for-profit transmission company, you have total separation.

Mr. LARGENT. I gotcha. Okay, thank you, Mr. Chairman.

Mr. BILIRAKIS. Mr. Hall, do you have a further question for these—the chairman is in the other room, and he wants to ask some questions, and—he does not prefer to go into a second round.

Mr. HALL. You mean, he wants a round and——

Mr. BILIRAKIS. No, his round—he hasn't had his round yet.

Mr. HALL. Well, we don't want one either.

Mr. BILIRAKIS. He wants to ask questions from the first round, but I am willing to recognize members of the panel for one question each, if they would like, until he comes in. I hereby recognize you.

Mr. HALL. Mr. Chairman, if we would be allowed to submit questions and the panel would agree to answer them within a week, because we may be marking this up in a week or 10 days.

Mr. BILIRAKIS. By all means. That of course is a request of the panel regarding all questions.

I would ask this then: Some charge that H.R. 2944 codifies the northern States power decision and balkanizes transmission regulation by providing for State regulation of the transmission used in retail sales—the subject we were on a few minutes ago that Mr. Largent went into. In your view, does H.R. 2944 codify the northern States decision or does it codify Order 888, and does it in fact balkanize transmission regulation?

Mr. Chairman?

Mr. HOECKER. In my view, my reading of the bill is that it codifies the jurisdictional call in 888. It doesn't necessarily codify the decision.

Mr. BILIRAKIS. Any further quick responses to that? Mr. Hebert? Mr. Massey?

Mr. MASSEY. Mr. Chairman, I would not legislate that division of authority. That is the call we made in Order 888, but it would concern me somewhat to legislate it, because I am not sure what flows from that, and it may be that it would lead to a further balkanization of the marketplace that we would see over time as things develop. So, my preference would be not to legislate that distinction between bundled and unbundled transactions.

Mr. BILIRAKIS. Mr. Hebert?

Mr. HEBERT. Thank you, Mr. Chairman. As to Northern States, I would have to agree with the chairman—I think it is a very close call. I don't know. It would be my thought initially that it does not codify the Northern States' case. However, when it comes to 888, it does not in fact codify 888, but what it does do is codify the authority to issue 888.

Mr. BILIRAKIS. Any further comments?

Ms. BREATHITT. With respect to bundled versus unbundled retail sales, I would think that at some point in time the other 25 States will probably make decisions to have retail open access, at which time there won't be any more bundled retail sales; that would go away. If you had it in the legislation, it may become outdated.

Mr. BILIRAKIS. Yes, well, it is an area that needs to be clarified, certainly.

Mr. Sawyer, do you have anything you want to offer?

Mr. Bryant?

Mr. Largent?

Mr. Chairman?

Mr. BARTON. Thank you, Mr. Chairman. I would like to ask my 5 minutes of questions now.

Mr. BILIRAKIS. By all means, please do so.

Mr. BARTON. I want to thank the entire Commission for being here this afternoon. I have a few fairly simple questions.

First, I want to ask if the Commission is generally supportive of the provisions in the current draft on Bonneville and the TVA in terms of FERC authority that is extended to those Federal utilities?

Mr. HOECKER. I am.

Ms. BREATHITT. I am.

Ms. BAILEY. I am, also.

Mr. MASSEY. Yes, I am too.

Mr. HEBERT. I am, Mr. Chairman, with the exception—I think what you are trying to accomplish is the right thing; however, I have told you privately, as well, I think the best way—and I understand bills are made of compromises—but the best way would be to sell of those transmissions assets to a jurisdictional utility instead of increasing the authority that FERC has.

Mr. BARTON. Okay, I understand that.

Second, we have got several members of the subcommittee on both sides of the aisle that are very concerned about FERC jurisdiction over the transmission system in terms of cooperatives and municipals. We have put in a small transmitting utility exemption. We also encourage distributed generation facilities. Currently, it is at 50 megawatts, and I am getting a lot of complaints that that is too big. Does the Commission have a number that you would feel comfortable with, if we took that from 50 megawatts and took it down to a smaller number? And if you do, I would sure like to hear your number.

Mr. HOECKER. Mr. Chairman, I know that I don't have a number. I think that interconnection for small distributed generation is certainly appropriate. I don't know what the feasible cutoff would be from a statutory perspective.

Mr. BARTON. Okay. Does the number 10 megawatts strike a bell with anybody? Or you just don't want to say?

Ms. BAILEY. I think from the standpoint of a 50 megawatt, I think there are some power plants that can be 50 megawatts, so that is why you are getting some feedback probably on that.

Mr. BARTON. Yes. And we realize that we have been too generous, and we—we, I; I am not going to blame the subcommittee for this. Okay.

What about the provisions we have put in on self-certification for cooperatives if they send a letter to the Commission that they are not FERC jurisdictional? Have you all—that they are not a transmission cooperative and they are not going to be FERC jurisdictional. We have tried to make that as simple and as easy as possible, because the cooperative said that they didn't have the funds to hire high-priced attorneys and things like this. Have you all looked at those provisions, and, if so, are those acceptable to the Commission?

Mr. HOECKER. Speaking for myself—we haven't talked—but we have instances in other statutes for self-certification, and I think that we could make that work. We have provided waivers from open access for small cooperative utilities even if they owned transmissions. So, it is something that we have some sympathy for.

Mr. BARTON. Okay. Three of you are former State regulators, and if I were to summarize the dispute between the subcommittee in terms of how to reach the goal of competition, there is one group that thinks we ought to defer as much as possible to the States and be as circumspect as possible in terms of additional authority at the Federal level. And that is where the current draft is. There is another group that feels like that we need more direct Federal intervention to get to the market that everybody supports.

In your opening statements, all of you were generally supportive of the thrust of the bill, which does not have a Federal mandate in terms of a date certain, and it does defer generally to the States in any area that it can. Are you all comfortable with that approach?

Mr. Hebert?

Mr. HEBERT. Mr. Chairman, if I may, the August 4 draft used the term "maximum practical deference" to the States, which I thought was preferable to the language of this one. I think you just the term "deference." So, if I had to choose the language of the two, being a former State legislator and State chairman, I would suggest that "maximum practical deference" would be preferable.

And a lot of that would have to do with which boulevard you take. Which end of the boulevard are you going down, and if you are going down the one which takes you toward mandates, then you probably don't want to give as much deference. But if you are going toward voluntary incentive-type systems and RTOs, then maximum practical deference I believe would work and be in the best interest.

Mr. BARTON. Any other Commissioner, Ms. Breathitt?

Ms. BREATHITT. I haven't read NARUC's comments that will be proffered soon by my friend, Marsha Smith from Idaho, but the history of the Commission working well with the States to work out the difficulties where our jurisdiction butts up against their jurisdiction, it is fairly well defined in the Federal Power Act. To be a little bit more direct, unless there is something that I don't know at this point, I think your current bill keeps those lines well divided.

Mr. BARTON. Last—oh, Mr. Chairman—Hoecker?

Mr. HOECKER. I just want to make an observation, Mr. Chairman. I don't think over the last half dozen years you will find a commission that is more deferential and accommodating to State interests. This integrated industry that we are talking about today affects both Federal and State interests profoundly, and we try to accommodate them in a variety of ways. We have been deferential in terms of their ability to recover stranded costs. We have been deferential in terms of their jurisdiction over bundled retail service. We are deferential in terms of their ability to regulate reliability at the retail level, and even in some transmission areas, I would be deferential. We are deferential in terms of their ability to have access to books and records if PUHCA is reformed. We are deferen-

tial in terms of how we try to facilitate retail competition. And we have really, I think, gone more than the extra mile in that regard.

But make no mistake about it, what we are talking about here is regulation of an interstate—of interstate commerce in electricity, and at some point I think there has to be a recognition that there is a large Federal interest at stake here and that we need to take action at the wholesale level to make competition happen.

Mr. BARTON. Mr. Hebert, and then my time is expired.

Mr. HEBERT. Mr. Chairman, just one other quick observation.

Mr. BARTON. We will let Ms. Bailey—Commissioner Bailey—we are going to give everybody a shot now. So, you all waited a long time. That is why we wanted all five of you here.

Mr. HEBERT. Just a quick observation. As you know, once we start arguing what the intent of Congress was or is, we have to look at clarifying language, and whatever you pass, if you do pass something, if you come out with deference, I can guarantee you there will be a day at the FERC, at the Commission table, where someone argues they didn't mean maximum, they mean practical, they just meant mere deference, because they had the opportunity to do something else.

Mr. BARTON. Okay.

Mr. HEBERT. Thank you.

Ms. BAILEY. Mr. Chairman, let me just suggest that the issue of deference is because traditionally, historically, the bulk of the jurisdiction has been with the States. The States are very critical to your vision and our vision of this competitive electricity competition bill and reliability legislation that you have here.

Legislation that just transfers more authority to FERC is not useful in this process, I think, to the extent that what you are seeing now is the result of successes of the initiatives that FERC has done and that should be built upon, and I think the States are at the point where they could help us do that. So, I am definitely in the camp where with cooperation and collaborative efforts with the States, I think is very necessary.

Mr. BARTON. Thank you. Thank you, Mr. Chairman.

Mr. BILIRAKIS. Thank you, Mr. Chairman.

I think we have completed the questioning from the panel here, and thanks so much. You have been very, very patient and very busy people, and you have sat here very patiently through these many hours. We appreciate it. You have been an awful lot of help.

Thanks, Mr. Chairman, and members of the Commission.

The next panel will also have been most patient. The Honorable Marsha Smith, commissioner of Idaho—with the Idaho Public Utilities Commission, representing the National Association of Regulatory Utility Commissioners, and Mr. Irwin "Sonny" Popowski, Pennsylvania Consumer Advocate Office of Consumer Advocate, Harrisburg, Pennsylvania, representing the National Association of State Utility Consumer Advocates.

If they would come forward, please.

Let us have a little bit of order. The hearing has not ended.

Your written testimony has already been presented and a part of the record, and I will set the clock at 5 minutes. Obviously, I won't cut you off if you go over it to some degree. You have been

very patient. We appreciate your taking the time, both of you, to be here.

And we will recognize Ms. Smith to present her testimony.

STATEMENTS OF MARSHA H. SMITH, COMMISSIONER, IDAHO PUBLIC UTILITIES COMMISSION, REPRESENTING THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS; AND IRWIN "SONNY" POPOWSKY, PENNSYLVANIA CONSUMER ADVOCATE OFFICE OF CONSUMER ADVOCATE, REPRESENTING THE NATIONAL ASSOCIATION OF STATE UTILITY CONSUMER ADVOCATES

Ms. SMITH. Mr. Chairman, thank you for this opportunity to be here today. I really appreciate it. And the first thing I want to say is to thank the chairman for his hard work on the bill that we are considering today and to thank the staff of the committee, the subcommittee, for being always available and attentive to listen to the State concerns, which have been many. So, we really appreciate your hard work.

This is a lengthy bill with many provisions, and of course it is not possible to address them all in 5 minutes, so I am going to hit on a few key provisions that are still very important to us.

First of all, we strongly support reliability legislation. There is a need to move from the current voluntary system to a mandatory system. Title II will have our unqualified support if a glaring omission is corrected. And that glaring omission is that there is no role for State policymakers in the process outlined. And there must be a role for the State policymakers in reliability. Who gets the calls when the lights go out because of transmission system trouble? Governors and State public utility commissions, that is who. It will not be acceptable to tell folks at home to call FERC or Congress or a national reliability organization. This is not only good policy but just plain common sense.

We propose two additions to the reliability section of the bill. Our proposed language is attached to my written testimony. First, we suggest a savings clause for those States which now exercise authority to ensure reliability. Don't take from the States, which already exercise their existing authority to deal with their specialized concerns.

Second, we suggest a statutory process for a State advisory role at the regional level. Recently, opponents of the advisory role have raised the specter that it will balkanize and be another layer of regulation. All you have to do is look at the successes in the western interconnection to know that the opposite effect will occur. This will be a process to efficiently and cooperatively address, at the regional level, the concerns that arise at a regional level. It is not another decisionmaker or level of regulation or bureaucracy.

The two provisions we propose have widespread support. You already have letters from numerous groups representing a wide variety of interests nationwide. Please add these provisions to the bill.

We really appreciate the evidence that our earlier comments were heard and that there is no mandate for States to implement retail competition by a date certain. Nearly half the States have acted to date; others will follow in an appropriate manner and at a time that is right for them. So, it makes little sense to us, and

we oppose the provisions of the bill that impose hard reciprocity. That is a detriment to States trying to create the most active and efficient retail competition.

Why limit the choices their consumers can enjoy? Why limit off-system revenues that can lower rates? If the purpose of the legislation is to lower consumer electric bills, then reciprocity does not belong in it. Furthermore, interconnections also go beyond national boundaries. So, to the extent that reciprocity is also imposed on an international basis, it causes difficulty for States that have boundaries with Canada and Mexico.

On distributed resources, I want to point out that many States are strong supporters of distributed resources and technologies, and some believe that those are the future of this industry. A 1998 NARUC resolution supporting greater consistency in terms and conditions of interconnection of small scale generating units demonstrates our support.

Unfortunately, the provisions of section 542, dealing with special rules for distributed generation, will not encourage or facilitate the development of these technologies. Instead, they are likely to create more problems and probably delay and hamper the deployment of distributed resources.

Interconnection on the local distribution level is a State and local concern. It has serious consequences for distribution reliability. FERC is not the correct entity to oversee these types of interconnections. The State commissions are in place to address these very local concerns, and will be able to do so faster and with better results, because they are aware of different concerns that may apply to different systems. A statement by Congress expressing a Federal policy to encourage distributed technologies would be positive. The provisions of section 542 may be disastrous. Public safety is at issue as well as electric reliability at the local level.

I am very pleased to see that responsibility for the formation of regional transmission organizations, or RTOs, has been placed on the industry and the regions. All of the regions of the Nation are actively engaged in forming or working toward forming the right regional body in terms of geographic scope and governance structure. I do share some of Commissioner Bailey's concerns with the dates that are in the bill and believe that they may not be realistic.

I would like to emphasize that State jurisdiction over retail services must be retained regardless of the facilities used. System maintenance, planning, and siting are core State responsibilities and must remain so. We are concerned with legislating the FERC's seven factor test out of Order 888. Instead, we urge a wholesale-retail test, a transaction test, not a wires classification test.

The bill could also be enhanced by the provisions to secure public benefits that may otherwise be lost. NARUC supports maintaining programs that support energy efficiency, renewable technology, research and development, universal service, and low-income assistance.

With that, Mr. Chairman, I would commend to you the written comments, which in more detail outline our concerns with the bill but recognizing that it is a good place to start.

[The prepared statement of Marsha H. Smith follows:]

PREPARED STATEMENT OF MARSHA SMITH, COMMISSIONER, IDAHO PUBLIC UTILITIES COMMISSION AND VICE CHAIR, NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

Mr. Chairman and Members of the Subcommittee: My name is Marsha Smith. I am a Commissioner on the Idaho Public Utilities Commission and Vice Chair of the National Association of Regulatory Utility Commissioners (NARUC) Committee on Electricity. I also serve NARUC as a member of the Ad Hoc Committee on Electric Industry Restructuring. In addition, I am Chair of the Committee on Regional Electric Power Cooperation (CREPC), a committee of the Western Interstate Energy Board (WIEB). WIEB is an organization of 12 western States and 3 Canadian Provinces. I respectfully request that NARUC's written statement be included in today's hearing record as if fully read.

NARUC is a quasi-governmental nonprofit organization founded in 1889. Within its membership are the governmental bodies of the fifty States engaged in the economic and safety regulation of carriers and utilities. The mission of NARUC is to serve the public interest by seeking to improve the quality and effectiveness of public regulation in America. More specifically, NARUC is comprised of those State officials charged with the duty of regulating the retail rates and services of electric, gas, water and telephone utilities operating within their respective jurisdictions. We have the obligation under State law to assure the establishment and maintenance of such energy utility services as may be required by the public convenience and necessity, and to ensure that such services are provided at rates and conditions which are just, reasonable and nondiscriminatory for all consumers.

I greatly appreciate the opportunity to appear on behalf of NARUC before the United States House of Representatives, Committee on Commerce, Subcommittee on Energy and Power regarding H.R. 2944, the "Electricity Competition and Reliability Act." I commend the Chairman for holding this hearing and for the work and effort by you and your staff to produce this legislation. NARUC and its members appreciate the complexities you have confronted while trying to get H.R. 2944 to this juncture. We would also like to thank you for your consideration of our views throughout this process and your efforts to reach a compromise on issues important to the States.

Since the beginning of the debate in Congress regarding electric industry restructuring NARUC has been guided by a set of basic principles in the transition to competitive retail electricity markets. A general theme of these principles is that the States should have jurisdiction over components of the competitive *retail* electricity market, including reliability and FERC jurisdiction should be focused upon components of the competitive *wholesale* electricity market. To this end our principles are intended to support State restructuring initiatives and to provide customer choice while ensuring the continued provision of adequate, safe, reliable and efficient energy services at fair and reasonable prices at the lowest long-term cost to society.

In light of the local impact that restructured retail markets will have, State commissions and legislatures should decide whether, when and how local markets should be opened to greater competition. We would like to express our appreciation for your decision to *not* include a date certain mandate in H.R. 2944.

A brief summary of NARUC's restructuring principles:

- The safety, reliability, quality and sustainability of services must be maintained or improved;
- All consumers must share the benefits of structural improvements and be protected from anti-competitive behavior, undue discrimination, poor service and unfair service practices;
- Public benefit programs must be maintained, including those which support energy efficiency, renewables technologies, research and development, universal service and low-income assistance; and
- States and State commissions must be afforded the flexibility to determine retail electric policies, including the content and pace of restructuring programs and retail stranded cost determinations.

Based on these basic goals, NARUC believes that Federal legislation could enhance restructuring initiatives by:

- Affirming State authority to order and implement retail access/customer choice programs free from the threat of preemption under the Commerce Clause or the Federal Power Act;
- Affirming States' authority to impose wires charges to support the recovery of stranded costs, State-sponsored energy efficiency and/or environmental and renewables programs, and universal service programs;

- Affirming States' authority to regulate retail power delivery services regardless of the facilities used, thereby eliminating the threat of customers bypassing the local distribution network;
- Reaffirming States' exclusive jurisdiction over the rates, terms and conditions of retail electric services, including retail transmission services;
- Authorizing the voluntary formation by States of regional regulatory bodies to enable States to address regional transmission and system operation concerns; and
- Reaffirming a State role in reliability.

I would now like to devote the remainder of my time to discussing H.R. 2944.

DISCUSSION OF PENDING LEGISLATION

Title I—Open Transmission Access

Section 101 of this Title provides that the States shall have the authority to require retail competition or unbundling of transmission and distribution. The Federal Energy Regulatory Commission (FERC) is given exclusive jurisdiction over unbundled retail transmission but is specifically denied jurisdiction over bundled retail sales of electricity subject to State regulation. The Section permits States to impose charges on retail services for public purpose programs. It also gives FERC the authority to determine whether a particular delivery facility is FERC jurisdictional or State jurisdictional, using the 7 factor test found in Order 888. When making this determination, FERC shall give "deference" to the position taken by the State.

NARUC supports the provision found in this section that affirms State authority to implement retail competition and is pleased that the bill denies FERC jurisdiction over bundled retail rates and services. However, we also support legislation that affirms *State* authority to regulate *retail* power delivery regardless of whether the facilities are transmission or distribution. Accordingly, while we applaud H.R. 2944 for preserving State authority over bundled services, we also support State authority to regulate all services provided retail consumers on an unbundled basis, including transmission.

Additionally, NARUC supports the provisions of H.R. 2944 that affirm State authority to: impose non-bypassable charges to support stranded benefits including implementation of programs to promote energy efficiency, renewable energy resources, and support for low income consumers; implement programs to promote energy efficiency and renewable energy resources, and to support low-income and rural consumers; and ensure that all market participants adhere to appropriate health, safety, reliability and consumer protection standards. However, NARUC also supports the inclusion in legislation of workable mechanisms to support State public benefits programs that consider a Federal-State partnership with broad-based competitively neutral funding mechanisms, and Federal support to assist and encourage the States to develop and implement public purpose programs that meet the needs of the States and the Nation. In addition, we continue to support funding for public purpose research and development programs based upon taxes and tax credits and non-bypassable system charges.

Concerning the identification of facilities as "transmission" or "distribution", NARUC has serious reservations regarding the workability of provisions in H.R. 2944 that codify the FERC Order 888 seven factor test. Application of this standard can hardly result in an intelligible "brightline" between State and Federal jurisdiction as the Supreme Court directed over 30 years ago. We believe that the retail/wholesale test removes uncertainty and avoids the need to categorize every piece of wire in the nation when it is necessary to draw the transmission/distribution distinction. NARUC also supports legislation that would authorize States to form voluntary regional bodies to define the character of transmission facilities.

In Section 102, the bill extends FERC jurisdiction to "transmission utilities" defined as "any entity (including State and municipality) that owns or operates facilities used for transmission" of electricity. The Section also authorizes FERC to address recovery of stranded wholesale costs.

NARUC has not taken a position on the extension of FERC jurisdiction to non-jurisdictional entities or wholesale stranded cost recovery. However, we would like to reiterate our opposition to FERC authority over the recovery of any retail stranded costs, an issue now being litigated in the United States Court of Appeals.

Section 102 also includes a provision that authorizes FERC to order retail transmission services on behalf of retail customers served by an open access distribution company. While NARUC does not have a specific position on this issue, in general we support Federal transmission policies that assist States in voluntarily opening retail markets.

Section 103 of H.R. 2944 requires transmitting utilities to establish or join a Regional Transmission Organization (RTO) by January 1, 2003. Under this section FERC may approve, but not require, the establishment of such RTOs. NARUC supports legislative language that leads to the voluntary formation of ISOs. However, we believe that legislation should clarify the authority of State and Federal regulators to require that transmission owners transfer control of systems to ISOs, where necessary to ensure a competitive market, in the event voluntary action is not effective. In addition, NARUC supports legislation authorizing formation of voluntary regional bodies to address transmission system issues.

This Section also includes a savings clause allowing State commissions to address transmission issues, including maintenance, planning and siting, "in a manner consistent with this Act and FERC decisions under this Act." We believe it to be fundamental that legislation regarding retail electric competition affirms the authority of States to regulate retail power delivery services *regardless* of facilities used. This provision, as drafted, does not meet this fundamental principle. Maintenance, planning and siting are core responsibilities of the States, and must remain so, and not to FERC jurisdiction under the FPA.

In Section 104 of this bill Congress authorizes the formation, under FERC approval and oversight, of interstate compacts for regional transmission siting. NARUC supports legislation authorizing formation of voluntary regional bodies to address transmission system issues such as the definition of transmission and distribution facilities, operation of transmission systems (including supervision of ISOs and PXs), system planning, transmission pricing and facilities siting. However, our policy on voluntary regional bodies does not contemplate FERC approval and oversight. Additionally, we believe transmission siting must remain State jurisdictional.

Section 105 of H.R. 2944 gives FERC authority to order the expansion of transmission facilities, subject to State and local laws concerning property rights and siting, upon utility application and requires FERC to convene a joint board for the purpose of receiving recommendations before transmission expansion may be ordered. NARUC has a long history of support for FERC authority to convene joint boards. However, NARUC does not support FERC authority to order expansion of transmission facilities if that authority preempts State authority over siting, system planning or retail power delivery services.

TITLE II—RELIABILITY

The reliability of the nation's electric system is one of the most important issues in this debate, and NARUC believes that Federal legislation must indeed address this subject. Federal legislation should facilitate effective decision-making by the States and authorize States to create regional mechanisms for the purpose of addressing transmission reliability issues.

NARUC cannot support reliability legislation that fails to provide a role for States in ensuring reliability of all aspects of electrical service, including generation and power delivery services, or results in FERC preemption of State authority to ensure safe and reliable service to retail consumers. To that end, we recently sent to the Subcommittee two amendments to the reliability title to safeguard State jurisdiction to secure safe, reliable and adequate service for retail consumers. These amendments included a savings clause to protect current State commission authority over retail service reliability except for actions that harmed reliability, and a provision to establish a voluntary regional body of State officials to advise industry-based reliability organizations. Unfortunately, neither amendment was included in H.R. 2944. While we appreciate inclusion of the bill's savings clause to protect State authority over *distribution*, it is clearly inadequate to remove legal clouds over State regulation of transmission-related issues.

We continue to urge the Subcommittee to include our amendments in this legislation. Further, we are prepared to consider alternative formulations of State role provisions as this legislation moves forward, whether as part of a broader bill or as a stand-alone reliability bill. However, the inclusion of no meaningful role for the States in addressing reliability issues is simply unacceptable.

NARUC, however, does support workable mechanisms to assist energy efficiency programs that enhance reliability. We believe that construction of new power lines is not the only way to strengthen our reliability system. All alternatives must be on the table, including initiatives on the customer's side of the meter.

In attachment 1 of this testimony, I have provided the Subcommittee with amendments that addresses the State's concerns.

TITLE III—CONSUMER PROTECTION

Section 301 requires that the Federal Trade Commission (FTC), in consultation with FERC, the Department of Energy (DOE), and the Environmental Protection Agency (EPA), issue rules for disclosure to retail consumers. NARUC supports initiatives leading to minimum, enforceable uniform standards for disclosure and labeling but believes that such activities should occur primarily at the State level. Therefore, NARUC would support consultation with State commissions as well as FERC, DOE and EPA in any legislation creating a Federal role.

Section 302 deals with consumer privacy issues, and while NARUC does not have a specific position on consumer privacy, NARUC believes that Federal legislation ought to affirm *State* jurisdiction over the terms and conditions of retail service.

Section 303 addresses FTC rules against slamming and cramming and a savings clause for State disclosure rules that "are not inconsistent with" FTC requirements. NARUC does not currently have a formal position on slamming/cramming issues but we would support language that affirms State authority to ensure adherence to consumer protection standard.

Section 304 expresses a sense of Congress that States should ensure universal service to all consumers. NARUC's principles on restructuring affirm our view that universal service must be maintained in all restructured markets.

TITLE IV—MERGERS

Section 401 modifies FERC's authority over mergers by adding time limits for decisionmaking, authorizes FERC to address mergers at the holding company level, and directs FERC to assess the impact of mergers on wholesale and retail markets. It also extends FERC's authority over disposition of utility assets to include direct authority over generating facilities rather than indirect authority over wholesale power supply.

NARUC supports a Federal merger policy where both Federal and State *regulators* (i.e. State commissions and the FERC) thoroughly evaluate mergers to assess their impact on competition, access to transmission and distribution facilities and ultimately on electric rates. We believe that the role of economic regulators should complement review by antitrust agencies to adequately protect the public against market power abuses. NARUC also supports merger policies where State commissions have primary responsibility to assess retail impacts of the merger. FERC should support the States in this regard, particularly when the State commissions in question lacks adequate State law authority.

TITLE V—PROMOTING COMPETITION

Sections 501 and 502 of H.R. 2944 would establish reciprocity provisions restricting sales into retail markets that are open to competition. NARUC opposes these reciprocity provisions. Reciprocity limits consumer choices and potential savings. Federally mandated reciprocity provision will result in harm to retail customers. In the case of a State with retail access, a reciprocity provision may remove potential suppliers of lower cost power. In a State without retail access, a reciprocity provision may eliminate opportunities for off " system revenues that could be used to reduce customers" rates. In either case, consumers are worse off under reciprocity.

In short, if the purpose of electric restructuring is to save money for electric consumers then a reciprocity provision should not be in the bill.

Sections 511-524 and 531-533 address PUHCA and PURPA. NARUC supports reform or repeal of PUHCA as competition becomes effective through comprehensive legislation. We support mechanisms that maintain State and Federal authority over holding company practices and preserves consumer protection provisions of recent legislation " the 1992 Energy Policy Act and the 1996 Telecommunications Act. NARUC also supports reversal of the *Ohio Power* decision and State access to books and records. We oppose the legislation's provisions that grant FERC authority to exempt holding companies and their affiliates from State books and records requirements.

With regard to PURPA, NARUC supports legislation to lift PURPA's purchase requirement where a State has made a finding that the acquisition of generating capacity is subject to competition or other acquisition procedures that protect the public interest with respect to price, service, reliability and diversity of resources. Additionally NARUC strongly opposes the provision in H.R. 2944 that grants FERC authority to preempt the States by ordering the recovery of costs in retail rates.

Section 541 authorizes aggregation of acquisition of power by retail consumers in open retail markets, "notwithstanding any provision of State law". NARUC has taken no specific position on aggregation, but in general supports exclusive State

authority over the regulation of rates, terms and conditions of retail electric services.

Section 542 requires FERC to issue regulations requiring a local distribution utility to interconnect with distributed generation facilities presumably preempting State interconnection policies. While NARUC believes that access to the electric supply market by small-scale distributed resources can offer important public benefits (mitigating market power, furthering innovation, easing transmission and distribution constraints, increasing resource diversity, and expanding customer choice), NARUC does not support FERC preemption of State interconnection policies. State commissions should be the agencies responsible for removing unnecessary barriers to interconnection.

TITLE VII—ENVIRONMENTAL PROVISIONS

Sections 701 and 702 establish a renewable energy production incentive, and provide for net metering, with a savings clause that permits the State to impose a cap on net metering. NARUC supports the inclusion of legislative provisions affirming a national commitment to continued commercialization and supply of renewables. If Congress adopts minimum national standards, such as a renewable portfolio standard, NARUC supports the use of tradable credits as one market-compatible mechanism to meet such standards. However, States should have flexibility to apply and supplement any Federal standards.

NARUC also believes that it is the role of State commissions and legislatures to choose to adopt net metering measures. It is the role of Congress and FERC to remove legal barriers to State implementation of net metering that may be contained in the Federal Power Act or PURPA.

TITLE VII—INTERNAL REVENUE CODE PROVISIONS

The only comment that we have with regard to this Title concerns Section 803. NARUC supports the provision to allow deductibility of decommissioning costs.

CONCLUSION

Mr. Chairman, in conclusion let me again thank you and your colleagues on the Subcommittee for allowing NARUC to participate in the legislative process, not only through my appearance here today, but in our informal discussions as well. Respectfully, let me state that we do not support the enactment of H.R. 2944 as currently drafted. The bill's failure to adequately provide a role for the States in the area of reliability is enough to require us to withhold our support at this time.

In 1978, Congress enacted five bills comprising the National Energy Act, which for the first time injected the Federal government into retail electric and natural gas service issues. Virtually all of those statutes, with the exception of PURPA, have been either repealed or consigned to irrelevancy. Congress is now poised to repeal PURPA, completing its repudiation of the 1978 legislation's involvement in retail utility markets.

We urge Congress to keep the lessons of the National Energy Act in mind as it considers further retail legislation. We strongly support the decision to abandon pursuit of the date-certain mandate. Having made that decision, we now urge you to focus the attention of the Congress on areas where new Federal laws can facilitate State restructuring efforts and on areas where the Federal government can work in partnership with the States to continue support for important public purposes such as R&D, low income assistance, renewable energy technologies, and energy efficiency.

If Congress chooses to act, Federal legislation should preserve broad State authority to implement these policies flexibly in response to the conditions in local retail markets. The development of retail customer choice should be implemented in a manner that respects these differences. In our view, that can only happen if decisionmakers closest to these conditions—State commissions and legislatures—enjoy the flexibility to adapt pro-competitive policies to the needs of local retail consumers. In the weeks and months ahead, I and my colleagues look forward to continue working with Congress and with all interested parties to develop workable policies that support an efficient and environmentally sound electric services industry that meets the needs of all retail customers.

I have provided two attachments to my written statement for your review and consideration. Attachment 1 is the NARUC supported reliability amendment for inclusion in Title II. Attachment 2 is an analysis of H.R. 2944 with NARUC supported policy statements for each Title and relevant sections.

ATTACHMENT 1

Amendments to NERC Reliability Legislation to Preserve State Role

Section (xx) – Savings Clause

Nothing in this section shall be construed to preempt the authority of a state to take action to ensure the reliability, adequacy, or safety of electric facilities within the state except where the exercise of such authority has a material adverse impact on the reliable operation of the bulk power system.

Proposed Report Language

Since the North American Electric Reliability Council was established in the mid-1960s, electric reliability standards and procedures were conducted through voluntary industry actions subject to the regulatory authority of State regulatory commissions. As a result, utility planning to ensure reliable service and the utility investments necessary to implement these plans were fully subject to review and approval by State regulators. This system gave the United States the most reliable electric services in the world, while allowing for State commissions to adapt North American reliability standards and procedures to local and regional needs and conditions.

The proposed reliability legislation would convert the voluntary program of the past to a self-regulatory reliability organization (SRRO) subject to the regulatory authority of the Federal Energy Regulatory Commission (FERC). It is not the intent of Congress that FERC's authority to approve reliability standards developed by the NAERO or take action to enforce compliance with such standards would displace the legitimate interests of the States in ensuring reliable electric services for their citizens. The purpose of this savings clause is to clarify that with the passage of this legislation, States retain authority under State law to take the following actions:

- establish and enforce standards to ensure the adequacy of electric facilities within the State;
- investigate and resolve complaints concerning the reliability of electric services;
- establish and implement procedures for emergency response to the failure of electricity facilities and services within the States;
- investigate the causes of the failure of electricity facilities and services within the State;
- establish and implement standards for the siting of electricity facilities within the State;
- establish and enforce standards to maintain and improve the quality and safety of electricity services provided within the State; and
- impose a charge upon entities providing electricity services within the State to recover the costs of ensuring safe, reliable and adequate services.

In addition, the savings clause would allow State commissions to take actions that strengthen the NAERO standards. State actions that materially adversely affected the application of the NAERO standards would not be permissible.

Section (yy) REGIONAL ADVISORY ROLE—

(1) ESTABLISHMENT- The Secretary of Energy shall establish a regional advisory body on the petition of the Governors of at least 2/3 of the States within a region that have more than 1/2 of their electrical loads served within the region.

(2) MEMBERSHIP- A regional advisory body-- (A) shall be composed of 1 member from each State in the region, appointed by the Governor of each State; and (B) may include representatives of agencies, States, and provinces outside the United States, on execution of an appropriate international agreement described in subsection (f).

(3) FUNCTIONS- A regional advisory body may provide advice to an affiliated regional reliability entity, the electric reliability organization, or the Commission regarding-- (A) the governance of an affiliated regional reliability entity existing or proposed within a region; (B) whether a standard proposed to apply within the region is just, reasonable, not unduly discriminatory or preferential, and in the public interest; and (C) whether fees proposed to be assessed within the region are—

(i) just, reasonable, not unduly discriminatory or preferential, and in the public interest; and

(ii) consistent with the requirements of subsection (l).

(4) DEFERENCE--ENTIRE INTERCONNECTION- In a case in which a regional advisory body encompasses an entire Interconnection, the Commission may give deference to the recommendations of the regional advisory body that are provided for in paragraph (3).

Proposed Report Language

It is the intention of Congress that States work together to develop regional approaches on electricity issues, in keeping with the regional nature of the interconnected high voltage transmission system. To the extent practicable, these regional efforts should be coordinated with the efforts of other regional institutions, especially those of the affiliated regional reliability entities, so that the advice from the regional bodies can receive effective consideration early in the process. Although the Commission may defer to the advice from an Interconnection-wide regional body, in most cases participants (including regional advisory bodies) should be able to resolve issues through the processes of the electric reliability organization and its regional affiliates.

ATTACHMENT 2

H.R. 2944, "The Electricity Competition and Reliability Act" Provisions Affecting State Regulatory Commissions

Title I – Open Transmission Access

Sec. 101 -- 1. State commissions can require retail competition and unbundling

NARUC supports legislation affirming State authority to implement retail competition

2. Exclusive jurisdiction over unbundled retail transmission goes to FERC

NARUC supports legislation affirming State authority to regulate retail power delivery regardless of facilities used (transmission or distribution). NARUC opposes the expansion of FERC jurisdiction to include unbundled retail transmission services

3. FERC is specifically denied jurisdiction over bundled retail sales of electricity (including any component thereof) subject to State regulation

NARUC supports legislation affirming State authority to regulate retail power delivery regardless of facilities used (transmission or distribution)

4. State commissions can impose charge on retail services for public purpose programs with nonexclusive list of purposes

NARUC supports legislation affirming State authority to impose non-bypassable charges and to promote energy efficiency, renewables, and low-income assistance. NARUC also supports the inclusion in legislation of workable mechanisms to support State public benefits programs that consider a Federal-State partnership, broad-based competitively neutral funding mechanisms, and Federal support. NARUC also supports funding for public purpose research and development programs based upon taxes and tax credits and non-bypassable system charges

5. A State commission, transmitting utility, or local distribution company may apply to FERC for decision as to character of power delivery facilities – i.e. whether transmission (FERC-jurisdictional)

or distribution (State-jurisdictional). FERC uses Order 888 7 factor test, but shall give deference to State positions

NARUC has expressed serious reservations concerning the workability of the Order 888 test. NARUC supports legislation to authorize States to form voluntary regional bodies to define the character of transmission facilities

Sec. 102 -- 1. Extends FERC jurisdiction to "transmitting utilities" defined as "any entity (including State or municipality) that owns or operates facilities used for transmission" of electricity and authorizes FERC to address recovery of stranded wholesale costs

NARUC has no position on the extension of FERC jurisdiction to non-jurisdictional entities (coops, munis, PMAs etc.) or wholesale stranded cost recovery. NARUC opposes FERC authority over the recovery of retail stranded costs

2. Authorizes FERC to order retail transmission services on behalf of retail customers served by an open access distribution company

NARUC has no specific position on this issue, but supports Federal transmission policies that assist States in voluntarily opening retail markets

3. Directs FERC to adopt rules to exempt small transmitting utilities (e.g. small municipal and cooperative systems) from open access requirements

NARUC has no position on this issue

Sec. 103 -- 1. Transmitting utilities required to establish or join RTOs by January 1, 2003. FERC may approve, but not require establishment of RTOs

NARUC supports legislation leading to the voluntary formation of ISOs, but in the event voluntary action is not effective, also supports consideration of legislation to clarify authority of State and Federal regulators to require that transmission owners transfer control of systems to ISOs where necessary to ensure a competitive market. NARUC supports legislation authorizing formation of voluntary regional bodies to address transmission system issues

2. Savings clause to allow State commission to address transmission issues (maintenance, planning, siting) "in a manner consistent with" the FPA and FERC decisions thereunder

NARUC supports legislation affirming the authority of States to regulate retail power delivery services regardless of facilities used

3. Directs FERC to encourage incentive transmission pricing policies

NARUC has no position on incentive pricing for transmission services, but has supported the use of cost-based methodologies in wholesale markets (primarily generation) that have not become fully competitive

Sec. 104 -- 1. Congress authorizes formation of interstate compacts for regional transmission siting

NARUC supports legislation authorizing formation of voluntary regional bodies to address transmission system issues such as the definition of transmission and distribution facilities, operation of transmission systems (including supervision of ISOs and PXs), system planning, transmission pricing and facilities siting. NARUC opposes preemption of State siting authority

2. FERC to determine whether State-proposed compact meets statutory requirements

NARUC's policy on voluntary regional bodies does not include FERC approval or oversight

3. FERC to issue rules to govern compact formation

NARUC's policy on voluntary regional bodies does not include FERC approval or oversight

Sec. 105 -- 1. FERC to order expansion of transmission facilities, subject to State and local laws concerning property rights and siting, upon utility application

NARUC does not support FERC authority to order expansion of transmission facilities if that authority preempts State

authority over siting, system planning or retail power delivery services

2. FERC must convene joint board to get recommendations before transmission expansion may be ordered

NARUC has a long history in support of FERC authority to convene joint boards under section 209 of the FPA

Title II – Reliability

Sec. 201 -- 1. Includes NERC "consensus" draft from February 1999 with some variations

NARUC supports legislation establishing mandatory compliance with industry-developed reliability standards and providing explicit authority to FERC and the States to cooperate to enforce those standards. NARUC also supports legislation that includes workable mechanisms to support energy efficiency programs that enhance reliability

2. Includes savings clause for State authority over reliability of local distribution facilities

NARUC cannot support reliability legislation that fails to provide a role for States in ensuring reliability of all aspects of electrical service, including generation and power delivery services or results in FERC preemption of State authority to ensure safe and reliable service to retail consumers. NARUC is concerned that a savings clause for local distribution could actually be harmful to State interest since it raises question that NERC might otherwise cover such issues and because it implicitly supports view that legislation preempts State regulation of non-distribution-related reliability issues

Title III – Consumer Protection

Sec. 301 -- 1. FTC to issue rules for disclosure to retail consumers – price, quality, other charges, generation source, emissions. Requires FTC to consult with FERC, DOE and EPA

NARUC supports initiatives leading to minimum, enforceable uniform standards for disclosure and labeling. NARUC supports consultation with State commissions as well

2. Savings clause for State disclosure rules that "are not inconsistent with" FTC requirements

NARUC urges States to include enforceable disclosure and labeling standards in retail access programs

Sec. 302 -- 1. FTC to issue rules to protect retail consumer privacy

2. Savings clause for State disclosure rules that "are not inconsistent with" FTC requirements

NARUC has no specific position on consumer privacy issues, but supports legislation that affirms exclusive State jurisdiction over terms and conditions of retail service

Sec. 303 -- 1. FTC to issue rules against slamming and cramming

2. Savings clause for State disclosure rules that "are not inconsistent with" FTC requirements

NARUC has no position on slamming/cramming issues but supports legislation affirming State authority to ensure adherence to consumer protection standards

Sec. 304 -- 1. Expresses sense of Congress that States should ensure universal service to all consumers, including rural, residential and low-income

NARUC's restructuring principles assert that universal service should be maintained

Title IV – Mergers

Sec. 401 -- 1. Modifies FERC's authority over mergers by adding time limits for decisionmaking. Authorizes FERC to address mergers at holding company level, and to assess impact of mergers on wholesale and retail markets

NARUC supports a Federal merger policy where both Federal and State regulators thoroughly evaluate mergers to assess

their impact on competition, access to transmission facilities and ultimately on electric rates. NARUC supports merger policy where State commissions assess retail impacts

2. Extends FERC's authority over disposition of utility assets to include direct authority over generating facilities rather than indirect authority over wholesale power supply

NARUC supports exclusive State authority over retail services and facilities

Title V – Promoting Competition

Sec. 501 -- 1. Establishes "hard reciprocity," i.e. no utility may sell to a retail consumer unless it's subject to competition in all its services territories or has applied to its State commission(s) to approve an open access plan (regardless of the State's decision to approve or disapprove) or has obtained a prior exemption from State reciprocity requirements

NARUC opposes legislation implementing hard reciprocity

Sec. 502 -- 1. Establishes international "hard reciprocity," i.e. no Canadian or Mexican utility may sell to a retail consumer in the U.S. unless it's subject to competition in all its retail operations

NARUC opposes legislation implementing hard reciprocity

Secs. 511-524-- 1. Repeals PUHCA 12 months after enactment using "standard provisions," i.e. FERC and State access to books and records where necessary to "identify costs", reversal of *Ohio Power* decision. Authorizes FERC to exempt holding companies from State books and records requirements

NARUC supports reform or repeal of PUHCA as competition becomes effective under comprehensive legislation. NARUC supports mechanism that maintains State and Federal authority over holding company practices and preserves consumer protection provisions of recent legislation – the 1992 Energy Policy Act and the 1996 Telecommunications Act. NARUC supports reversal of *Ohio Power* decision and State access to books and records. NARUC opposes granting FERC authority to exempt companies from State books and records requirements

Secs. 531-533 --

1. Prospectively repeals PURPA while preserving existing contracts

NARUC supports legislation to lift PURPA's purchase requirement where a State determines that generating markets are competitive or that the public interest in resource acquisition is protected

2. FERC to issue regulations preempting State authority over recovery of PURPA contract costs

NARUC opposes FERC authority to order the recovery of costs in retail rates

Sec. 541 --

1. Authorizes aggregation of acquisition of power by retail consumers "notwithstanding any provision of State law" in States with open retail markets

NARUC has no position on aggregation, but supports exclusive State authority over the regulation of rates, terms and conditions of retail electric services

Sec. 542 --

1. FERC to issue regulations requiring local distribution utility to interconnect with distributed generation facilities, presume preemption of State interconnection policies

NARUC urges State commissions to remove unnecessary barriers to interconnection

Title VI – Federal Utility Provisions (TVA, BPA)

1. Extends FERC authority to transmission systems, wholesale power sales of Federal utilities

2. Establishes other conditions on operation of Federal utilities

NARUC has no position on these issues

Title VII – Environmental Provisions

Sec. 701 -- 1. Establishes renewable energy production incentive of 1.5 cents per kwh to solar, wind, biomass and geothermal technologies owned by public entities (municipalities, coops)

NARUC supports inclusion of legislative provisions affirming national commitment to continued commercialization and supply of renewables. If Congress adopts minimum national standards, NARUC supports use of tradeable credits as one market-compatible mechanism, among others. State should have flexibility to apply and supplement any Federal standards

Sec. 702 -- 1. Requires retail electric suppliers to provide net metering services

2. Savings clause for State requirements "consistent with the requirements in this section". Allows State to impose cap on net metering

NARUC urges State commissions and legislatures to adopt net metering measures and requests Congress and FERC to remove barriers to State implementation of net metering

Title VIII – Internal Revenue Code Provisions

Sec. 801 -- 1. Removes tax restrictions on co-ops provision of open access transmission services, retail competition

NARUC has no position on this issue

Sec. 802 -- 1. Removes "private use" restrictions on tax-exempt bonds of municipal systems providing open access transmission, ISO membership, retail competition

NARUC has no position on this issue

Sec. 803 -- 1. Allows deductions of nuclear decommissioning costs by utility subject to non-cost-based regulation

NARUC supports legislation to allow deductibility of decommission costs in restructured utility industry

Sec. 804 -- 1. Extends the renewable energy tax credit for wind and closed-loop biomass

NARUC has supported production tax credit for renewable technologies

Title IX – Miscellaneous Provisions

Sec. 901 -- 1. DOE to prepare report to Congress in 2 years on actions taken by States to remove barriers to interstate commerce in electricity and recommendations for further congressional action

NARUC has no position on this issue

Mr. BILIRAKIS. Thank you. Thank you very much for all that, Ms. Smith.

Mr. Popowsky, please proceed.

STATEMENT OF IRWIN "SONNY" POPOWSKY

Mr. POPOWSKY. Thank you, Mr. Chairman.

My name is Sonny Popowski. I am the consumer advocate of Pennsylvania, and I am testifying on behalf of the National Association of State Utility Consumer Advocates, or NASUCA. NASUCA is an organization of State utility consumer advocate offices from 39 States and the District of Columbia. We are charged by our respective State laws with representing utility consumers before State and Federal regulatory agencies, courts, and legislative bodies.

First, I would like to thank Chairman Barton and the members and staff of this subcommittee for consistently seeking the input of NASUCA members as representatives of retail electric consumers in our respective States in each step of your deliberations. We heartily endorse your efforts to ensure that the voices of the consumers who ultimately will pay the bill for electric restructuring are heard in this debate.

We believe that the success of your efforts in this monumental task will be judged not by the size of the financial gain to any particular segment of the electric industry but rather by the impact on the reliability and price of electric service to America's electricity consumers.

With respect to the first two questions that the witnesses were asked to address, the need for Federal legislation and the necessary components of such legislation, NASUCA agrees that Federal legislation is required in at least two areas: reliability and market power. But as I and other members of NASUCA have testified on several prior occasions, we do not believe that a Federal mandate for retail electric competition in all States by a date certain is either necessary or appropriate.

We believe that the individual States are in the best position to determine whether and when to open up their electric industries to one of the various forms of retail electric competition that are being implemented today in numerous States. On the other hand, NASUCA members recognize the limitations of State authority and therefore the need for Federal legislation in such areas as reliability and market power.

With respect to reliability, I have had the honor to serve for the last 2 years as 1 of 2 consumer representatives on the Board of Trustees of the North American Electric Reliability Council, or NERC. I believe that NERC is an outstanding organization that has done a magnificent job of maintaining the reliability of our Nation's electric system, but as the members of NERC and virtually all industry participants agree, the basic voluntary structure of NERC cannot be sustained in an increasingly competitive electric industry.

There is a need for Federal legislation to establish an independent electric reliability organization that can develop and enforce mandatory reliability rules subject to the oversight of the FERC. NASUCA supports Federal legislation that would accomplish this goal, such as the language contained in H.R. 2944, with the caveat that such legislation must clearly preserve the role of States in maintaining the reliability, safety, and adequacy of electric service within their State's borders.

With respect to market power, NASUCA supports Federal legislation that would strengthen the ability of the FERC to ensure open, fair, and non-discriminatory access to transmission facilities. Federal legislation should give FERC clear authority to monitor the development of competitive markets and the authority to take necessary steps to remedy anti-competitive abuses. We would respectfully suggest that H.R. 2944 be amended to include stronger market power provisions, such as those included in H.R. 2050, which was introduced by Mr. Largent and Mr. Markey and in the administration bill.

Now, H.R. 2944 requires the establishment of regional transmission organizations, or RTOs, but does not give FERC the direct authority to establish such organizations. In addition, while the legislation properly requires that the RTO must be independent of market participants, the section goes on to state that the independence requirement can be met, for example, even if a market participant owns as much as 10 percent of the voting interest in the RTO.

NASUCA would urge the elimination of such exceptions to the independence requirement, as they could lead to the domination of RTO governance by a particular industry segment. The hallmark of a successful RTO in NASUCA's view is total independence from the financial interests of any particular market participant or market segment.

NASUCA also submits that additional transmission pricing incentives are not necessary in order to encourage the development of competitively neutral, independent RTOs.

In addition to the need to address market reliability and market power, NASUCA would also support Federal legislation that establishes basic standards for consumer protection and universal service as long as such standards do not preempt efforts of the States to provide stronger protections and universal service benefits to consumers.

Finally, in this regard, NASUCA would note that consumers' efforts in achieving competitive benefits at the Federal level would be enhanced by the establishment of a FERC Office of Consumer Council. The establishment of such an office was included in the

August 4, 1999 discussion draft that was submitted to this subcommittee but was not included in H.R. 2944, as introduced.

Now, in my prepared written testimony, I have compared some of the specific provisions of H.R. 2944 to the consumer checklist for Federal legislation that was presented to this subcommittee by NASUCA president, Fred Schmidt, on July 22, 1999. And we hope that you will keep these principles in mind as you go forward with the legislative process.

Again, NASUCA appreciates the opportunity to comment on this bill and on the principles that we believe should be contained in any Federal electric restructuring legislation. We look forward to continuing to work with you, the members of the committee, and your staff in developing policies and legislation that will truly benefit all consumers.

Thank you.

[The prepared statement of Irwin "Sonny" Popowsky follows:]

PREPARED STATEMENT OF SONNY POPOWSKY, CONSUMER ADVOCATE OF THE COMMONWEALTH OF PENNSYLVANIA ON BEHALF OF THE NATIONAL ASSOCIATION OF STATE UTILITY CONSUMER ADVOCATES

Chairman Barton and members of the Subcommittee on Energy and Power: My name is Sonny Popowsky. I am the Consumer Advocate of Pennsylvania and the Immediate Past President of the National Association of State Utility Consumer Advocates (NASUCA). NASUCA is an organization of state utility consumer advocate offices from 39 states and the District of Columbia, charged by their respective state laws with representing utility consumers before state and federal regulatory agencies, courts, and legislative bodies. I have been asked by you to testify on behalf of NASUCA regarding 1) the need for federal electricity legislation; 2) the specific elements that should be included in any federal legislation; and 3) the provisions of H.R. 2944, the Electricity Competition and Reliability Act of 1999, that are of particular interest to NASUCA.

Before addressing these questions, I would like to thank Chairman Barton and the members and staff of this Subcommittee for consistently seeking the input of NASUCA members, as representatives of retail electric consumers in our respective states, in each step of your deliberations. While we do not necessarily agree with all of the provisions of H.R. 2944 or, for that matter, any of the legislative proposals that have been introduced in this Congress, we heartily endorse your efforts to ensure that the voices of the consumers who ultimately will pay the bill for electric restructuring are heard in this debate. We believe that the success of your efforts in this monumental task will be judged not by the size of the financial gain to any particular segment of the electric industry, but rather by the impact on the reliability and price of electric service to America's electricity consumers.

With respect to your first two questions—the need for federal legislation and the necessary components of such legislation—NASUCA agrees that federal legislation is required in at least two areas: reliability and market power.

As I and other members of NASUCA have testified before the House and the Senate on several prior occasions, we do not believe that a federal mandate for retail electric competition in all states by a date certain is either necessary or appropriate. We believe that the individual states are in the best position to determine whether and when to open up their electric industries to one of the various forms of retail electric competition that are being implemented today in numerous states. On the other hand, NASUCA members recognize the limitations of state authority and therefore the need for federal legislation in such areas as reliability and market power.

With respect to reliability, I have had the honor to serve for the last two years as one of two consumer representatives on the Board of Trustees of the North American Electric Reliability Council (NERC). I believe that NERC is an outstanding organization that has done a magnificent job of maintaining the reliability of our Nation's electric system. But as the members of NERC and virtually all industry participants agree, the basic voluntary structure of NERC cannot be sustained in an increasingly competitive electric industry. There is a need for federal legislation to establish an independent electric reliability organization that can develop and enforce mandatory reliability rules, subject to the oversight of the Federal Energy Reg-

ulatory Commission (FERC). NASUCA has endorsed legislative language that would accomplish this goal, with the caveat that such legislation must preserve the role of states in maintaining the reliability, safety and adequacy of electric service within their state's borders.

NASUCA also supports federal legislation that would strengthen the ability of the FERC to ensure open, fair and non-discriminatory access to transmission facilities, including authority to establish independent and competitively neutral regional transmission organizations. Federal legislation should give FERC the authority to monitor the development of competitive markets and to remedy anti-competitive abuses.

In addition to the need to address reliability and market power, NASUCA would also support federal legislation that establishes basic standards for consumer protection and universal service, as long as such standards do not preempt efforts of individual states to provide stronger protections and universal service benefits to consumers.

Finally, in this regard, NASUCA would note that consumers' efforts in achieving competitive benefits at the federal level would be enhanced by the establishment of a FERC Office of Consumer Counsel. The establishment of such an Office was included in the August 4, 1999, Discussion Draft that was submitted to this Subcommittee, but was not included in H.R. 2944 as introduced. NASUCA would urge that the creation of such an office be included in any final legislation that addresses electric restructuring at the federal level.

Turning to the specific provisions of H.R. 2944 that are of greatest interest to NASUCA, I would like to compare those provisions to the "Consumer Checklist" for federal legislation that was presented to this Subcommittee in testimony presented by NASUCA President Fred Schmidt of Nevada on July 22, 1999. As stated by Mr. Schmidt, the NASUCA Consumer Checklist represents a roster of principles that we believe should be reflected in any federal legislation to ensure that electric restructuring benefits, rather than harms, consumers. Those principles and the extent to which we believe they are consistent with the provisions of H.R. 2944, are set forth as follows:

1. **Federal Preemption:** *Federal legislation should permit states to adopt retail competition statutes or rules. There should not be a federal mandate for states to require retail competition by a date certain.*

H.R. 2944 does not mandate retail competition by a date certain. NASUCA fully supports the decision to leave this fundamental decision to the states.

2. **Stranded Costs:** *Retail stranded cost issues should be left to states.*

H.R. 2944 generally leaves stranded cost issues to the states. NASUCA supports this reservation of critical state authority.

3. **Market Power:** *Legislation should provide FERC with specific authority to monitor the development of competitive markets, to eliminate undue concentrations of market power in any relevant market, and to remedy anticompetitive conduct or the abuse of market power by any player, incumbents, affiliates, or new market entrants. These powers should include the authority to order divestiture or other structural remedies when necessary.*

NASUCA respectfully submits that H.R. 2944 does not adequately address market power issues. NASUCA strongly urges that market power provisions such as those included in the Administration Bill, H.R. 1828, and the Largent/Markey Bill, H.R. 2050 be included in any final legislation.

4. **Transmission and ISOs:** *Legislation should authorize FERC to require ISOs or other independent and competitively-neutral regional transmission operation organizations. Legislation should authorize FERC to rectify transmission policies, practices or prices which create a competitive advantage for services offered by the transmission provider or affiliates.*

H.R. 2944 requires the establishment of regional transmission organizations (RTOs) by transmitting utilities by January 1, 2003, but does not give FERC the authority to establish such organizations. In addition, while the legislation, in Section 103 properly requires that the RTO must be independent of market participants, this section goes on to state that the independence requirement can be met, for example, even if a market participant maintains passive ownership or owns as much as 10 percent of the voting interest in the RTO. NASUCA would strongly urge the elimination of such exceptions to the independence requirement from market participants as they could easily lead to the domination of RTO governance by a particular industry segment. The hallmark of a successful RTO in NASUCA's view is total independence from the financial interests of any particular market partici-

pant or market segment. NASUCA also submits that additional transmission pricing "incentives" are not necessary or appropriate in order to encourage the development of competitively neutral independent RTOs.

5. Reliability: *Legislation should authorize FERC to review the reliability requirements imposed by an independent North American Reliability Organization to promote reliability of electric supply.*

H.R. 2944 contains a reliability section similar to that endorsed by NERC and a number of utility organizations. NASUCA supports the language with the addition of a savings clause clarifying that states have a vital role in maintaining the reliability, safety and adequacy of electric systems within each state's borders. The savings clause in Section 201 of H.R. 2944 is inadequate because it only refers to state jurisdiction over local distribution facilities.

6. Consumer Protection: *Legislation by Congress should adopt provisions which would set minimum standards for basic consumer protections. States should retain authority to set additional or more stringent or more specific standards.*

The draft includes many of the protections suggested by NASUCA, including protection from cramming and slamming, consumer privacy, and supplier information disclosure. NASUCA would support additional provisions that would establish minimum federal standards in such areas as credit collection activities and service quality standards. In all such cases, these federal standards should be viewed as floors that can be strengthened by state actions to protect consumers.

7. Universal Service: *Legislation should adopt universal service standards and principles as part of any restructuring.*

The legislation appropriately includes a sense of the Congress that every retail customer should have access to electric energy at reasonable and affordable rates. The legislation does not contain specific standards or principles in this regard, however. NASUCA would seek to work with members of this Subcommittee to develop provisions that would insure that all Americans can have access to safe, affordable electric service.

8. Aggregation: *Aggregation of small customers should be encouraged. Federal legislation should not preclude states from facilitating the aggregation of small customers by any entity.*

H.R. 2944 contains language clarifying the authority of municipalities and other entities to aggregate retail customers. NASUCA submits that all barriers to such aggregation efforts should be eliminated.

9. Mergers: *Legislation should specifically revise merger standards to require a net benefit to consumers. Legislation should expand FERC merger authority to include combinations that are currently outside FERC jurisdiction, such as electric communications and electric-gas mergers.*

NASUCA would respectfully urge stronger FERC review authority over mergers, including language that would require mergers to provide a net benefit to consumers.

10. PUHCA: *PUHCA should be addressed only as part of comprehensive restructuring legislation. Waiver of certain PUHCA provisions should be conditioned on holding companies (i) being subject to effective competition in every state in which they operate, or (ii) divesting all of their generation assets. In addition, legislation should provide FERC with current PUHCA authority to review affiliate transactions, provide state and federal access to books and records, and limit diversification.*

The legislation does include repeal of PUHCA as part of comprehensive restructuring legislation and provides state and federal access to books and records. It does not, however condition repeal on the existence of competition or divestiture of generation assets or provide FERC with current PUHCA authority to limit diversification.

11. PURPA: *Legislation should not waive Section 210, the PURPA mandatory purchase obligation, unless protections are in place to insure that utility generation is subject to effective competition.*

PURPA is repealed, but there are no provisions insuring that utility generation is subject to effective competition.

Again, NASUCA appreciates this opportunity to comment not only on H.R. 2944, but on the overall principles that we believe should be contained in any federal restructuring legislation. We look forward to continuing to work with you in developing policies and legislation that will truly benefit all consumers.

Mr. BILIRAKIS. Thank you very much, Mr. Popowsky.

Ms. Smith—well, I guess, maybe to both of you—I would just say that through our subcommittee's review of electric restructuring, I have stressed—and I might add that the chairman was always willing to listen—that any restructuring legislation must take into account the unique factors that exist in each State.

For instance, in my home State of Florida, Florida is a peninsula with interconnections to other States only along our northern border. Florida's electrical loads are concentrated in central and southeast Florida, but much of the generation is in the north, which means that there is a dominant north to south flow of power and not a uniform flow of power in all directions. Florida has no generating fuels native to the State. All fuels have to be brought into the State—oil, coal, nuclear, and natural gas. Florida's vulnerability to natural disasters, such as hurricanes, pose an additional threat to our State's electric system, and I might just add that approximately 90 percent of our consumers are residential consumers as it gets to business or industrial, if you will, and I know that that figure probably applies to a few other States, but I would say that that is kind of a unique feature as attributable to Florida.

So, I guess my question goes—and you can see I would like to think that you can see that utility restructuring would present under those kind of circumstances many challenges to a State that would have those unique factors. So, the question that I would have is do you think that this bill, as it now is written, preserves a State's ability or Florida's ability or any States' ability to deal with each of the unique characteristics adequately?

Ms. Smith?

Ms. SMITH. Well, Mr. Chairman, I guess that is why we strongly advocate the addition of our savings clause and our State advisory role with the reliability section. You know me, I have been here before stressing how unique the Northwest is, and that is true. And that is why I strongly believe that we have to work together as regions and as interconnections.

There is no national electric grid. There is a western interconnection grid; there is ERCOT. If Texas didn't want to be part of the Union electrically, they don't have to be. And then there is the eastern interconnection, which I am sure from your point of view looks a little different than from mine in the West where I look east and I see one interconnection.

So, that is why I strongly advocate that as a way to preserve a policymakers input into processes that will be important in terms of reliability.

Mr. BILIRAKIS. Mr. Popowsky, do you have——

Mr. POPOWSKY. I would agree. I think that is the best example of where you, particularly a State like Florida, would want to be careful to ensure that as long as you are not operating in a way that is inconsistent with Federal reliability standards in some way that would harm interstate commerce, certainly the issues that are faced by the Florida commission and all of you in Florida, with respect to reliability, you want to turn to your commission and turn to your State government first. So, we would support the concept that the legislation should include language that would preserve the role of the States in reliability.

Similarly, with respect to—generally, with respect to issues like consumer protections universal service, we think that there is a role for the Federal law to play in developing basic standards, but we think that the States ought to be permitted to enhance those protections on behalf of their consumers.

Mr. BILIRAKIS. And you speak on behalf of NASUCA when you say that.

Mr. POPOWSKY. Yes.

Mr. BILIRAKIS. Thank you.

Mr. Sawyer, to inquire.

Mr. SAWYER. Thank you, Mr. Chairman.

You both have been strongly recommended to me to answer the question that I have been asking this afternoon: how best to preserve an appropriate State role in terms of siting decisions for transmission, while making sure that reluctant States, or those who see no internal benefit, are not in a position to impede the development and evolution of a sound regional grid.

Ms. SMITH. Well, Mr. Sawyer, I think I sound like a broken record. I think the answer does lie in a regional approach through a properly formed RTO with the State advisory body, and I think in our interconnection, I think everyone sees the necessity of working together, because we are interconnected, and an Idaho power path in eastern Idaho has operating limitations placed on it, because if it puts too much power over it, a path in southern California goes down. So, we understand that we are interconnected.

We also have an active wholesale market in north-south transfers of power. So, it is beneficial to all of us when power can move north and south, and it moves both directions depending on the time of the year and the load.

So, from my view in the West, the answer lies in having a strong regional body with State advisory role so that all——

Mr. SAWYER. Who should create that region?

Ms. SMITH. No——

Mr. SAWYER. Not no, who?

Ms. SMITH. Oh, who? I thought you said, ''Should you?'' Well, I think your voluntary—your approach is correct to allow the industry in the first instance to work it out. It is a struggle, and I won't try and minimize the struggle that it is. And we are going through it now. We just had an all-day meeting on what kind of government structure is appropriate, and there wasn't a resolution yet, but we are working on it. I believe the Midwest, the Northeast, I think all regions are working on that, and I think eventually the right answer, depending on physical operation of the system and the market where trading and buying and selling is occurring, will emerge.

Mr. SAWYER. Mr. Popowsky, you are representing a State just—a hypothetical State that is not a participant, and you nonetheless are the locus of a proposed transmission facility. How best should your State's voice be preserved without standing in the way of the ability of surrounding States to benefit from this investment?

Mr. POPOWSKY. That is not as hypothetical a question as you suggest, and I think there were some people who thought that there ought to be a power line from Ohio to New Jersey, and that those of us in Pennsylvania who had a little problem with that were being provincial.

Mr. SAWYER. I wasn't thinking of any State in particular.

Mr. POPOWSKY. But I think that the planning—and I agree with Commissioner Smith—I think the planning, and I think the prior witnesses said that the planning has to be done on a regional basis. We are in this together. We have to try to develop regional transmission plans that benefit all of us in Ohio, New Jersey, Pennsylvania, Maryland.

The problem then becomes once you develop a regional plan, when you get to the actual physical siting, I don't think you can take that authority away from the people who are closest to where that line is going to be sited. That was really one of the big problems in Pennsylvania. Even if you have an agreement that there ought to be a power line, when you decide whose orchard it goes through, whose historic sites it runs through, whose neighborhoods, that is an issue that I think has to be decided at the State level, and hopefully if we have regional plans that benefit everyone, then we can—those local concerns can be accommodated, but I think the actual physical siting still has to be done at the State level.

Mr. SAWYER. Is there a Federal role in that to resolve differences?

Mr. POPOWSKY. I think there can be a Federal role in facilitating that regional—the regional planning issues and the regional development issues. I think that if people perceive that there is a benefit overall to these kinds of improvements in the transmission facilities, then they might get built better, but I think that you still need to—when you draw that line, you need to—that final decision has to be made at the State level.

Mr. SAWYER. Thank you, Mr. Chairman.

Mr. LARGENT [presiding]. I am going to yield myself 5 minutes since it was my turn.

Commissioner Smith, you talked about the States, 24 States, have move forward. When will we see the State of Idaho move forward with electricity restructuring?

Ms. SMITH. That cold day in Hell?

Mr. LARGENT. Ah. Gosh, I read all your testimony about wanting to induce competition, what is wrong with Idaho? We can't have competition there?

Ms. SMITH. Well, when you sit with the lowest rates in the country and there are no studies to show you will be better off, it is difficult to get your legislature to move anywhere but back.

Mr. LARGENT. What are the rates for Idaho?

Ms. SMITH. Our residential customers generally pay less than 5 cents a kilowatt hour.

Mr. LARGENT. Okay.

Ms. SMITH. Our industrial customers are less than two.

Mr. LARGENT. Your residential customers are 5 cents per kilowatt hour?

Ms. SMITH. Yes.

Mr. LARGENT. What is Oklahoma? Six? About six. And we have already moved forward. So, well, I guess I just wanted to kind of place some of your comments and your testimony in context with what is actually taking place in Idaho, which is awfully cold in Idaho.

Ms. SMITH. Well, I am here to testify on behalf of States of the Nation generally as represented by the NARUC.

The other important consideration that you have to understand, when you talk about electric power in Idaho, you are also talking about our water resources in the Snake River and water rights, and nothing brings people out of their chairs faster than the idea that existing water rights may be altered by some change in the operation of the dams on the river. So, it is much more complicated than the price of power for our State, and I think it is going to take us a lot longer to work those——

Mr. LARGENT. Can you, as a State commissioner in Idaho, deal effectively with Bonneville issues or is that something that has to be done at the Federal level?

Ms. SMITH. Mr. Chairman, that has to be done at the Federal level. There is a Northwest Power Planning Council which has members appointed by the four Northwest States, but they don't have real regulatory authority over Bonneville.

Mr. LARGENT. One of your comments that you have said that "NARUC can't support H.R. 2944, as it is currently drafted. The bill's failure to adequately provide a role for the States in the area of reliability is enough to require us to withhold our support at this time." Could you explain that? I mean, I guess I heard Mr. Popowsky on the one hand say that we needed to have mandatory reliability standards, and——

Ms. SMITH. And I agree with him on that.

Mr. LARGENT. Okay, so what are you talking about?

Ms. SMITH. I am talking about adding the two provisions—a State savings clause and the State advisory role. And language is attached to my testimony. We have been working on it for the last year and a half. I think there is still some work going on on just exactly how the savings clause should read, but the State advisory role language is nailed down pretty good. It has strong support. NERC does not oppose it and thinks its inclusion could be beneficial. So, I think those are the two provisions that we are speaking of on the reliability section.

Mr. LARGENT. Well, does it make sense to have 50 different reliability standards on a grid that we are trying to say is a national grid? I mean, we now have the capacity to wheel electricity across State lines. Does it make sense to have 50 different reliability standards?

Ms. SMITH. No, it wouldn't, Mr. Chairman, and that is not what we are advocating. If you read the State advisory role language, it would empower Governors to appoint members, and if those State policy people could agree on an interconnection-wide proposal or recommendation, then we would ask FERC to give that deference, but that is a very specialized circumstance, and that is why I am saying it is a process whereby regional concerns can get solved at the regional level more efficiently than they could be solved at the Federal level.

Mr. LARGENT. If in Federal legislation there is provisions that provide for non-bypassable fees that could be used for everything from universal service or environmental issues or low-income heating, why do we have to have Federal language specifying public benefits? I guess what I heard in your testimony was, on the one

hand, you don't trust the Federal Government to do anything; leave it up to the States. But when it came to public benefits funds, and there was renewables and some other issues, you want the Federal Government to jump in there and make sure that we get that in.

Ms. SMITH. Well, Mr. Chairman, I hope I didn't say we don't trust the Federal Government not to do anything, but I did say that we encourage and NARUC supports workable measures to encourage energy efficiency, encourage the development of renewables technologies, to keep research and development going, and to promote universal service and have low-income assistance.

Mr. LARGENT. The States don't do that?

Ms. SMITH. Some States do do that, not all States.

Mr. LARGENT. Does your State do it?

Ms. SMITH. We have never seen the need to have low-income assistance other than on a voluntary basis where customers choose to add extra dollars to their bills.

Mr. LARGENT. What about public benefits?

Ms. SMITH. I guess, by public benefits—well, we have energy efficiency programs. We have low-income weatherization programs, those types of things, yes.

Mr. LARGENT. So, you basically have tailored something that fits Idaho?

Ms. SMITH. Yes, but what has happened in the Northwest is we have moved away from a State-by-State approach, and we now have a regional approach in the Northwest Energy Efficiency Association, NEEA. So, we do it on a regional basis now.

Mr. LARGENT. You like having it on a regional basis.

Ms. SMITH. Yes. I think if you are looking toward the markets of the future, you want to have these on a regional basis.

Mr. LARGENT. And wouldn't that be preferable to a national basis?

Ms. SMITH. I think we would appreciate the support of the Federal Government in implementing those programs, and some of them, frankly, would have national, applicable——

Mr. LARGENT. So one size fits all.

Ms. SMITH. No, not necessarily.

Mr. LARGENT. Oh, okay. Well, my time has expired.

Gentleman from California.

Mr. ROGAN. Mr. Chairman, thank you.

Following up on the chairman's federalism issue, it raised a point there have been a number of people that have suggested that any consumer protection legislation ought not be dealt with on the Federal side; it ought to be left up to the States. And I am just wondering, Mr. Popowsky, what are your feelings about that?

Mr. POPOWSKY. We would have no objection to Federal legislation that would establish minimum basic standards at the Federal level for some of the issues that are addressed in 2944, like slamming and cramming. We would just want to make sure that those standards could be enhanced and supplemented at the State level to address specific State concerns so that States would not be preempted from having additional protections for consumers in those areas.

Mr. ROGAN. Your suggestion would be that in Federal legislation there essentially be a floor established——

Mr. POPOWSKY. That is right.

Mr. ROGAN. [continuing] that States could not go under but were free to buildupon.

Mr. POPOWSKY. That is correct.

Mr. ROGAN. Are there any other areas that you would want to see addressed in Federal legislation?

Mr. POPOWSKY. Well, as I said in my testimony, I think we need Federal legislation on the reliability issue, again, with the caveat that there are specific State issues that have to be addressed at the State level, and we would also support market power provisions that would address market power problems at the wholesale level that could not be addressed by individual States.

Mr. ROGAN. Ms. Smith, do you want to weigh in on that?

Ms. SMITH. No.

Mr. ROGAN. I wish everybody was as brief in their answers as you are, and, in fact, Mr. Chairman, on that happy note, I will yield back. Thank you.

Mr. BARTON I thank the gentleman from California.

Now, Mr. Sawyer, have you asked questions? Okay.

The Chair would recognize himself for the last 5 minutes of questions.

Mrs. Smith, welcome for the second time to the subcommittee on this issue. Have you studied or your association studied the Bonneville title of the draft before us?

Ms. SMITH. Mr. Chairman, I haven't specifically.

Mr. BARTON. Okay. You are aware, though, that it is what the region—you said you believe in regionalism, and I assume you are aware that we put in what your region wanted on Bonneville.

Ms. SMITH. If you did that, then I shouldn't comment.

Mr. BARTON. Okay. So, you should say something nice about that part of our bill.

Ms. SMITH. Thank you very much.

Mr. BARTON. There you go. Okay.

And I am told that in terms of the specific policy items that NARUC has put on the table, we have addressed every one in a positive way except the issue of States setting their own reliability standards. Can you tell me how many States currently set their own reliability standards?

Ms. SMITH. Mr. Chairman, I don't know that States specifically set their own reliability standards.

Mr. BARTON. Well, they don't, except for one.

Ms. SMITH. Is that New York?

Mr. BARTON. The Empire State.

Ms. SMITH. Yes. Well, they have specific concerns with the little island we call Manhattan.

Mr. BARTON. But, I mean, should we let one tail, even a big tail like the Empire State, wag the entire 49 other, or 47 other States, if we exclude Alaska and Hawaii, in terms of State reliability standard setting? Shouldn't we go with the 49 as opposed to the 1 State and then try to address that on a specific basis?

Ms. SMITH. I think, Mr. Chairman, that it may—there may be other States that also exercise some local reliability concerns, and I think there is probably room in the process, particularly if it is built around regions and RTOs.

Mr. BARTON. We encourage participation in RTOs.

Ms. SMITH. Yes. And I believe that kind of a structure will allow room to accommodate——

Mr. BARTON. And we allow for regional standards in the current draft. So, I think we are——

Ms. SMITH. I think we are——

Mr. BARTON. [continuing] same page there.

Ms. SMITH. [continuing] kind of on the same page.

Mr. BARTON. Yes.

Ms. SMITH. We would like to see the——

Mr. BARTON. I think we are not only on the same page, I think we are in the same paragraph. We are not just maybe on the exact sentence structure.

Ms. SMITH. That is true.

Mr. BARTON. Okay.

Mr. Popowsky—am I saying that right?

Mr. POPOWSKY. Yes, that is right.

Mr. BARTON. Oh, good. The consumer protections in the bill, I assume you have looked at those?

Mr. POPOWSKY. Yes.

Mr. BARTON. I am getting some feedback. I just had a meeting with one of the members of the subcommittee, and they are expressing kind of a generic unease, but when I ask for specific changes to improve the consumer protection, I have not been given any definitive proposals. I did not read your testimony, so you may have had some specifics in there. Could you elaborate on any enhanced consumer protection that you might feel we need to put in the next draft before we go to markup?

Mr. POPOWSKY. Well, basically, there were some additional areas that were in our comments that we filed at the last meeting concerning, for example, credit and collection standards, service quality standards. Mainly the point is, as what I tried to make with Mr. Rogan, which is that we support the idea that the FTC should be able to establish consumer protection standards at the Federal level. We think they could be expanded in a couple of the areas that we cited in our testimonies, but it is important to us also that they be viewed as floors rather than as ceilings, and we volunteer in our testimony to work with the committee to determine if there are any other specific provisions that are necessary.

Mr. BARTON. Okay, now we have some input that we ought to drop consumer protection from the Federal title, because that is something the States can handle. I happen to believe we ought to have some Federal consumer protection items in the bill, as does Chairman Bliley. He is very strong on that.

But to take the devil's advocate position, would your association accept if we were to drop as a Federal item the consumer protection and just put some language in that says we encourage States to take up that gauntlet?

Mr. POPOWSKY. No, we would prefer the approach—the general approach that you have taken, which is to identify consumer protections that ought to be recognized at the Federal level, use those as a floor, and perhaps to expand the categories that you have covered in your testimony—I am sorry, in your bill, rather than drop it. That would be our preference, as long as it is a floor, not a ceiling.

Mr. BARTON. Okay. I have got one more question; I want to make sure I understand it before I ask it.

The staff has asked me to ask a question about State aggregation rights, and I am not sure I totally understand it. But should the States, in your opinion, Mr. Popowsky—it has been a long day—be able to discriminate against aggregators? For example, should the State of Texas be able to bar cooperatives from aggregating and the State of Louisiana be able to give municipalities a preference by allowing forced aggregation?

Now, I don't understand what I just asked you, so if you don't understand it either, we are even. But there is apparently a concern about States doing aggregation different in different States if we don't have Federal aggregation language, which we do have in our current draft.

Mr. POPOWSKY. Generally, I would—our position is we would like to eliminate any barriers, certainly any barriers to aggregation. Beyond that, we are not looking to have a Federal rule, I think, that would force aggregation. We would look to—we think different States have done it differently. I think many of our members have a preference for what is called opt-out aggregation where a municipality could aggregate its consumers and then have them opt-out of that. But the key here is to make sure that there are no unnecessary, in fact, no barriers to aggregation.

Mr. BARTON. What if a State has a State barrier against aggregation? Should the Federal Government preempt that State aggregation provision in this legislation?

Mr. POPOWSKY. I don't think NASUCA has addressed that, but at this point we would just say that there should certainly be no Federal barriers to aggregation. We also have resolutions that would support dropping State—we would encourage States to drop those barriers. I can't say that we have—that we would ask the Federal Government to step in——

Mr. BARTON. So, if we, in order to foster competition and to foster the creation of markets, if we had a Federal preemption against State aggregation barriers—I am beginning to understand my question now—your association would at least be neutral and could possibly be supportive of that.

Mr. POPOWSKY. I would say we don't have a position on that, because it just—that particular question hasn't come up. Like I said, we would support of elimination of Federal barriers on aggregation——

Mr. BARTON. I got what you——

Mr. POPOWSKY. [continuing] and we would like to eliminate State barriers as well.

Mr. BARTON. There are no Federal barriers on aggregation, but we want you to help us take down some of these State barriers against aggregation.

Mr. POPOWSKY. Well, we would be happy to work with you on that, if you are aware of——

Mr. BARTON. Okay, that is a good answer.

Mr. POPOWSKY. Thank you.

Mr. BARTON. Okay. Does Mr. Pickering wish to ask questions of this panel?

Mr. POPOWSKY. I have no further questions.

Mr. BARTON. Does Mr. Sawyer have one last question? Okay, does Mr. Rogan? Okay.

We want to thank you two panelists. We are going to continue our hearing tomorrow, I believe at 10 a.m., and we have two panels, each has 6 or 7 people—9 and 8. Okay, so we are going to have a long day of enlightenment tomorrow from the private sector.

The hearing is recessed until 10 a.m. tomorrow morning in this room.

[Whereupon, at 4:15 p.m., the subcommittee recessed, to reconvene at 10 a.m., Wednesday, October 6, 1999.]

[Additional material submitted for the record follows:]

RESPONSES OF HON. JAMES HOECKER TO QUESTIONS FROM JOE BARTON, CHAIRMAN, SUBCOMMITTEE ON ENERGY AND POWER

Question 1. H.R. 2944 clarifies Federal and State jurisdiction, providing for FERC jurisdiction over transmission used for unbundled retail sales, and for State jurisdiction over transmission used for bundled retail sales. Is this clarification needed, and does the bill draw the jurisdictional line properly?

Response. On its face, the Federal Power Act (FPA) assigns the Commission jurisdiction over all facilities for the transmission of electric energy in interstate commerce by public utilities. Nevertheless, consistent with the historical practice of including the costs of transmission used to service retail markets or "native load" in state-regulated bundled retail rates, Order No. 888 held that the Commission has jurisdiction over transmission used for unbundled retail sales, and that States have authority over transmission used for bundled retail sales. It was the Commission's view that, until the advent of retail competition where transmission becomes "unbundled," this was the most workable arrangement. These determinations, made in 1996, are currently pending before the Court of Appeals for the District of Columbia Circuit.

As I view it, H.R. 2944 seeks to codify this 1996 interpretation. I believe that codification of the Commission's jurisdiction over transmission used for unbundled retail sales is appropriate. Such jurisdiction is necessary to ensure that all unbundled transmission is provided on a comparable basis to all users of the bulk power grid and to avoid balkanization of transmission access, with different interstate transmission rules established by each state that moves to retail choice.

However, codification of State jurisdiction over bundled retail transmission is appropriate only if it is accompanied by other legislative language that ensures the Commission's ability to require non-discrimination in the uses of the transmission grid. Regrettably, the Commission's stance in Order No. 888 is now being used to hamper its ability to ensure comparable transmission services for *all* uses of the grid, including service to native load. A recent appellate court decision may have placed a jurisdictional cloud over the Commission's authority to achieve Order No. 888's goals of non-discrimination in the provision of transmission services. *See Northern States Power Co., et al., v. FERC,* No. 98-3000 (8th Cir., May 14, 1999, *rehearing denied,* September 1, 1999) (*NSP*). This decision, if interpreted and applied broadly, may allow the States—through their jurisdiction over transmission used for bundled retail sales—to establish preferential terms and conditions for the bundled transmission services they regulate compared to the terms and conditions available to other transmission users. In other words, the historical regulatory practice enshrined in Order No. 888 of treating transmission used as part of a native load service differently from transmission used for other bulk power transactions, including service to other utilities' native load, makes demonstrably less sense in a competitive wholesale marketplace.

There are two ways to address the potential problems that could arise from the *NSP* decision. The first is to add a specific provision to H.R. 2944 to clarify the Commission's authority to ensure that transmission services within its exclusive jurisdiction are provided on a basis that is comparable to, *i.e.*, no less favorable than, other transmission services provided by a transmitting utility. This clarification is necessary to remove the potential for future balkanization of the interstate transmission grid. Accordingly, my testimony suggested revising Section 101 of H.R. 2944 to add a provision at the end of FPA section 201(a), as modified by section 101(b)(1) of the bill, stating that:

> In regulating the transmission of electric energy under any provision of this Part [Part II of the FPA], the Commission shall have exclusive authority to es-

tablish rates, terms and conditions of transmission service that are just, reasonable and not unduly discriminatory or preferential, including rates, terms and conditions that prevent or eliminate undue discrimination or preference associated with a public utility's or transmitting utility's own uses of its transmission system to serve its wholesale and retail electric energy customers.

This approach to addressing the *NSP* comparability problem is necessary if H.R. 2944 codifies State authority over bundled retail transmission or if the bill is silent on this matter.

The second way to address the *NSP* problem is not to codify State jurisdiction over bundled retail transmission and instead to expressly grant the Commission authority over all transmission, including what is now called bundled transmission. While the Commission's interpretation of State jurisdiction in Order No. 888 reflected an analysis of existing law and a recognition of the long-standing historical role of states in regulating transmission associated with retail sales, the industry has evolved significantly since Order No. 888 was issued. If dual (Federal-State) regulation of the transmission system results in a State-mandated preference for bundled transmission services and the balkanization of transmission access, with different rules established by each State and by the Commission, the Congress should need to broaden the Commission's jurisdiction to address this problem. It is my understanding that a legislative amendment has been proposed by the Americans for Affordable Electricity that would take this approach and make my proposed clarification unnecessary.

In sum, I urge the Congress to avoid further litigation and potential transmission discrimination problems by, at a minimum, adopting my proposed revision to section 101(b)(1) of H.R. 2944. Alternatively, the Congress may want to consider explicitly giving the Commission jurisdiction over all transmission, including transmission used for bundled retail sales.

Question 2. In your view, does section 102(a)(2) of H.R. 2944 amend section 212(h) of the Federal Power Act to authorize FERC to order retail wheeling to a consumer served by local distribution facilities in closed States? Is there a need to clarify the definition of "open access" in the legislation?

Response. I interpret section 102(a)(2) as authorizing the Commission to order retail wheeling only to consumers in those states that have required their utilities to provide open access over the utilities' local distribution facilities, i.e., to consumers in those states that have adopted retail choice. Of course, retail wheeling to these consumers may require wheeling by utilities in closed states and I interpret H.R. 2944 as allowing the Commission to order this service. The cited provision states that, notwithstanding the existing provisions of section 212(h)(2), "the Commission may issue an order that requires the transmission of electric energy directly or indirectly to retail electric consumers who are served by local distribution facilities that are subject to open access." The bill defines "open access" with respect to local distribution facilities as meaning that the "local distribution company that owns, controls, or operates the facilities offers not unduly discriminatory or preferential access to the facilities." The bill does not alter the states' authority to decide whether or not to order retail open access. Transmission "open access" should be given the meaning the Commission gave it in Order No. 888.

Question 3. Some charge transmission owners are redesignating transmission facilities as distribution facilities in order to avoid FERC open access requirements. Have you seen examples of such efforts by utilities? Are these utility efforts being supported by State public utility commissions?

Response. As retail competition is implemented, there arises a need to draw a distinction between transmission and local distribution facilities. Several utilities in various states have filed with the Commission proposals to classify certain facilities as either transmission or local distribution. Consistent with Order No. 888, each of these proposals was reviewed previously by the relevant State public utility commission as to the appropriate classification. Order No. 888 prescribed a general seven-factor test which defines what types of facilities would constitute transmission facilities subject to Commission jurisdiction or local distribution facilities subject to State jurisdiction. The Commission has issued six orders granting deference to State commissions who properly adopted the seven factor test. These cases did not involve substantial reclassifications.

Recently, the Commission has received four cases involving application of the seven-factor test by the State of Illinois. These involve substantial reclassifications to local distribution and the Commission is still reviewing these proposals. If a proposed reclassification could impair the availability of open access services, the Commission would be concerned and would consider this possible adverse effect in evaluating the proposed reclassification.

Question 4. H.R. 2944 includes an exemption from FERC regulation for small transmission owners. Do you believe this exemption is appropriate? Do you have any comments on the specific exemption provisions in H.R. 2944?

Response. Section 102(b) of H.R. 2944 would require the Commission to adopt rules allowing an exemption from Commission regulation for certain transmitting utilities. The bill lists certain criteria for exemption, which are similar to the Commission's criteria for waiving Order Nos. 888 and 889, and would allow the revocation of an exemption in the event of changed circumstances. The bill also specifies streamlined procedures for applicants to seek and obtain an exemption.

The bill's exemption provisions are reasonable. While the Commission is strongly committed to the policies of open access transmission services and competition in wholesale markets, I believe H.R. 2944's exemption provisions can be implemented without undermining those policies.

Question 5. FERC does not regulate transmission systems operated by State and municipal utilities and cooperatives, which are some of the largest systems in the country. State and municipal utilities oppose FERC regulation of transmission rates, and want to retain that authority. If State and municipal utility transmission systems continue to be unregulated could they shift power costs onto their transmission rates? Could they discriminate against competitors?

Response. With the exception of services ordered under section 211, transmission systems owned by state utilities, municipal utilities and cooperative-owned utilities are self-regulated or are regulated by a state agency such as the public utility commission or public service commission. If such a utility were to charge other users more than its own cost of transmission, it would result in discriminatory rates for other users. When such a utility charges competitors more for transmission than it charges itself, it would give the utility's generation a competitive advantage that was not based on actual differences in generation cost.

In Order No. 888, the Commission addressed the potential for such cross-subsidization and discrimination by public utilities. The Commission required public utilities to offer transmission service to others at the same rates, terms and conditions that public utilities apply to themselves, and to take Commission-jurisdictional services under the same tariff available to others. This "comparability" requirement is an important tool in preventing public utilities from using their control of transmission facilities to discriminate against their competitors in power markets.

As a matter of clarification, let me address several concerns that I have heard voiced about proposed FERC jurisdiction over municipally- and cooperatively-owned transmission. First, most public power entities do not own transmission and depend on open access to the transmission of others. Second, some cooperatives are concerned about potential interference in their local distribution functions. The Commission has no interest in regulating in that area. Third, a primary concern of many transmission-owning public power entities is the threat to tax-exempt financing that open access and federal rate regulation represent. I believe that all transmission should be operated under the same rules, and that the tax rules should be adjusted to accommodate that result. Finally, some small cooperatives and municipally-owned utilities have raised concerns about the cost of FERC regulation. I believe the provisions of H.R. 2944 concerning exemptions for small transmission owners reasonably address this concern in a manner that is consistent with our open access policies.

Question 6. Should FERC regulate transmission that is not in interstate commerce—such as transmission in noncontiguous States and territories?

Response. Transmission that is not in interstate commerce consists principally of two types of transmission. First, such transmission includes transmission within noncontiguous States and territories, such as Alaska and Hawaii. While I do not object to Congress giving the Commission the authority to regulate the rates, terms, and conditions of transmission within noncontiguous States and territories, I do not believe that it is essential for the Commission to have such authority. It is essential that all interconnected transmitting utilities be subject to the same transmission "rules of the road," and that all electricity suppliers have access to a single, seamless transmission grid over which to transact business. This is what allows wholesale buyers and sellers of electricity to have choices. Within the lower 48 States, where the transmission systems are interconnected, the Commission's pro-competitive regulation is necessary to achieve this end.

Second, the Commission has historically construed the transmission of electric energy wholly within the Electric Reliability Council of Texas (ERCOT) as not being in interstate commerce, and thus has treated the utilities performing such transmission as not being public utilities so long as they do not otherwise engage in Commission-jurisdictional activities. Two of the four investor-owned ERCOT utilities (West Texas Utilities Company and Central Power and Light Company) operate

both within and outside ERCOT and are public utilities subject to the FPA. The other two investor-owned utilities in ERCOT, Houston Lighting & Power (HL&P) and Texas Utilities Electric Company (TU), are not considered public utilities. A settlement agreement approved by the Commission in 1987 under section 211 of the FPA required certain ERCOT utilities to construct specified asynchronous direct current interconnections between utilities in ERCOT and utilities in the Southwest Power Pool. *Central Power and Light Co., et al.*, 40 FERC ¶61,077 (1987). A provision in the order approving the settlement stated that "HL&P and TU shall use the HVDC interconnections for any purpose, including the purchase, sale, exchange, wheeling, coordination, commingling or transfer of electric power and energy in interstate commerce." A section 211 order does not subject a utility to Commission jurisdiction for any other purpose. Thus, unlike similar entities elsewhere in the country, these utilities are not considered public utilities under sections 205 and 206 of the FPA.

In my testimony before the Subcommittee, I noted that H.R. 2944 would narrow even further the Commission's limited authority over ERCOT transmitting utilities—by denying the Commission the authority under section 211 of the Federal Power Act (as amended by the Energy Policy Act of 1992) to order transmission by those utilities that otherwise transmit only within ERCOT. In my testimony, however, I also stated: "I believe that all transmitting utilities should be subject to the same transmission rules. Open access to a seamless transmission grid by all electricity suppliers is essential if the Congress and the Commission intend to guarantee that buyers and sellers of electricity have as many choices as possible." I urge that the Congress at least retain the limited authority that the Commission presently has under section 211 of the Federal Power Act with respect to ERCOT utilities.

Question 7. NARUC proposed amending the reliability title of H.R. 2944 to authorize individual States to establish reliability standards. What is your position on this proposal? How many States regulate transmission reliability? Would 50 different reliability standards improve reliability? How would 50 different standards affect interstate commerce?

Response. The NARUC proposal, as drafted, would reserve to States the right "to take action to ensure the reliability, adequacy, or safety of electric facilities within the state except where the exercise of such authority has a material adverse impact on the reliable operation of the bulk power grid." This proposal is broader than H.R. 2944's provision, which would preserve existing State authority over *local distribution facilities* unless the exercise of such authority would unreasonably impair the reliability of the bulk power system. Of the two approaches, I find H.R. 2944's provision to be more appropriate. However, I also believe that Federal legislation could preserve for the States certain reliability practices that they have historically engaged in with respect to bundled transmission in their jurisdictions. Federal reliability laws should ensure that such State practices are consistent with the applicable regional or national standards and that such reliability practices do not unduly impair competition in bulk power markets.

According to a recent survey by the North American Electric Reliability Council (NERC), three states have specific jurisdiction over bulk power grid security and operation and have established reliability standards through the Regional Reliability Councils. Moreover, many states have maintenance and inspection standards for transmission facilities, and some states establish generation reserve requirements. Again, these measures are developed in coordination with the Regional Reliability Councils.

I do not read the reliability language included in H.R. 2944, even without the NARUC savings clause, as preempting those legitimate State roles. States would still be able to act to protect the reliability of local distribution, but they must do so consistent with the rules that apply across the transmission system. Having said that, I emphasize that it is essential that rules be established on a regional basis (as they are now) in order to prevent one state from inadvertently interfering with the reliability of service or the resource decisions made by retail customers in another state. Fifty different sets of reliability standards could create problems for interstate commerce and for maintenance of grid reliability. Individual states cannot guarantee reliability of the interstate grid.

Question 8. What is your view of the transmission pricing provisions of the bill introduced by Mr. Sawyer (H.R. 2786)?

Response. Section 5 of H.R. 2786 would add a new section 215 to the FPA. This section would require the Commission to permit recovery of all costs associated with transmission service, including expansion costs. It also would require consideration of costs and benefits to interconnected transmission systems caused by the creation of a regional transmission organization (RTO). Under H.R. 2786, rates, terms and

conditions must promote economically efficient transmission, the expansion of transmission networks, the introduction of new transmission technologies and provision of transmission services by RTOs, prevent cost shifting to rates for services outside the jurisdiction of the Commission, and be just and reasonable and not unduly discriminatory.

The Commission is further required by the proposed legislation to issue a rule within 180 days of enactment that would provide incentives to transmitting utilities to promote the voluntary participation and formation of RTOs without having the effect of forcing utilities to join, and extend such incentives to existing RTOs, limit the charging of multiple rates for transmission service, provided that a transition mechanism or period is allowed, minimize shifting of costs among existing customers, encourage efficient and reliable operation of the grid through congestion management, performance-based ratemaking, or incentive rates, and encourage efficient and adequate investment and expansion of the transmission system.

The bill would require the Commission to allow negotiated rates, and would allow the Commission to grant market-based rates only where it finds that relevant geographic and product markets for transmission services or for delivered wholesale power are subject to effective competition.

I believe the pro-competitive objectives of Mr. Sawyer's transmission ratemaking provisions are appropriate and laudable. I subscribe to the notions that we should incent economically efficient behaviors by utilities, prevent cost shifting, and encourage transmission owners to alleviate, not prolong, system congestion and alleviate rate pancaking.

I nevertheless believe that the transmission pricing provisions of H.R. 2786 may be too prescriptive. The standards under the FPA already allow the Commission to consider most, if not all, of the issues addressed in H.R. 2786 (*e.g.*, incentives for utilities to join RTOs, congestion management, performance-based ratemaking, enlargement of adequate transmission investment). However, the FPA gives the Commission flexibility to determine appropriate ratemaking methodologies that are just, reasonable and not unduly discriminatory. This flexibility allows the Commission to craft rate approaches that suit specific facts and companies, and which will most effectively reduce the role of regulation in a competitive market.

Several provisions of H.R. 2786, however, could be construed to preclude the Commission from adequately protecting transmission users. For example, the bill requires the Commission to allow negotiated transmission rates and prescribes a specific test for market-based transmission rates. In addition, the bill can be read to require rates that harm ratepayers because it appears to require recovery of all costs incurred, even those that were imprudently incurred. Under current law, the Commission does not permit recovery of imprudently incurred costs. I believe that these provisions could unduly hamper the Commission in its efforts to protect competition and consumers.

I am also concerned that over-emphasis on creating incentives to expand the grid may lead to distortion of the market, where alternatives to expansion, such as construction of new generation or investment in energy efficiency technologies, would cost less. Again, this is an issue that calls for fact-specific consideration and solutions.

I believe that appropriate incentives can be structured to create the proper market signals under current law. The Commission is exploring just such incentives in our Notice of Proposed Rulemaking, RM99-2.

Question 9. Some criticize the length of FERC merger proceedings. How long does it take FERC to approve mergers?

Response. The Commission has been highly responsive to the increasing number of requests for merger authorization. In December 1996, the Commission issued its Merger Policy Statement, and made a commitment to act on mergers within 90 days of the close of a 60-day public comment period, or within 150 days total. Since making that commitment, the Commission has received 31 merger applications and acted on 24 of them (setting three for hearing). One application was withdrawn and the other six have been filed only recently. The Commission has met its target of action within 150 days consistently. In fact, in a number of cases, the Commission has acted much more quickly.

As noted, the Commission set only three of these 24 cases for hearing. The cases set for hearing generally involved mergers of large utilities, with potentially significant effects on competition, and raised genuine issues of material facts.

Question 10. H.R. 2944 amends section 203 of the Federal Power Act to expand FERC review of sales of power plants and transmission facilities by State and municipal utilities, cooperatives, and federal electric utilities. Currently, those sales are not subject to review by FERC, DOJ, or FTC. Is there a need for federal review of these sales to ensure market power issues are addressed?

Response. Your question contains two elements: (1) whether the Commission needs jurisdiction over transfers of generating facilities; and (2) whether the Commission needs authority to review transfers of facilities by non-public utilities.

As to first aspect of the question, I believe that this Commission should have direct jurisdiction over transfers of generation facilities. Concentration of generation assets may directly and seriously affect competition in wholesale markets, and our review of such transactions is critical to protect the public interest. I discuss this further in my answer to Question 11, below.

As to the second aspect of the question, the Commission has not requested an expansion of its jurisdiction to cover review of transfers of facilities by non-public utilities. I would note that the Commission has jurisdiction under section 203 over a public utility's purchase or sale of jurisdictional facilities, an authority which would apply to some transfers of facilities by non-public utilities to public utilities and *vice versa*. Apart from these circumstances, Commission review of facility transfers among non-public utilities could also help to protect the public interest in competitive markets. The generation and transmission assets of certain non-public utilities are extensive, and the sale and redeployment of these assets could adversely affect competition, depending on the extent of other facilities controlled by the acquirer and on other circumstances.

Question 11. The Burr bill (H.R. 67) and the Sawyer bill (H.R. 2786) repeal section 203 of the Federal Power Act. What is your view of this proposal?

Response. I strongly oppose repeal of section 203. This authority is an essential element of the Commission's pro-competitive policy. In reviewing a merger, the Commission assesses the effects on competition, on rates, and on regulation. In most cases, the primary issue is the effect on competition. Consistent with its overarching goal of promoting competition in wholesale power markets, the Commission seeks to ensure that mergers will not harm competition. If a merger is likely to harm competition, mitigation of this potential harm is required in order to ensure that the merger is consistent with the public interest. Under this authority, the Commission has prevented competitive harm by providing other market participants with access to the transmission facilities of the merger applicants, thus ensuring that the merger does not reduce the competitive options available to wholesale buyers and sellers. Similarly, the Commission has accepted commitments by applicants to turn over control of their transmission facilities to independent system operators (ISOs), as a way of ensuring the merger did not cause competitive harm. The Commission also has required rate protection for captive customers. These and other conditions and commitments imposed or accepted by the Commission have provided substantial benefits to the public and, thus, ensured that the mergers were consistent with the public interest.

Although some have argued that our review is unnecessary in light of the authority of the Department of Justice and the Federal Trade Commission, I do not agree; this Commission's expertise and its role in working with energy markets distinguishes it from the functions of antitrust enforcers. Our day-to-day involvement with the electric industry gives us a valuable and detailed understanding of electricity markets as they are shaped by the transmission grid. This expertise can provide critical insights in assessing a merger's effects on competition. Second, this Commission's authority to protect the public interest encompasses not only the effect of a transaction on competition, but also its effects on the rates consumers pay. Since certain aspects of the electric power industry, such as transmission, are not subject to effective competition, the broader scope of the inquiry conducted by the Commission helps to protect consumers from effects not considered by the antitrust agencies. Third, our procedures permit public participation in a timely process to determine the public interest, in a way antitrust enforcement does not. This public review process remains important in today's electric industry, given the vital importance of the industry to American citizens and the national economy.

Question 12: H.R. 2944 allows TVA to sell wholesale power outside the region but provides for FERC regulation of such sales. Could TVA get FERC approval to charge market-based rates for these sales?

Response. The Commission has explained in a number of cases in recent years the criteria that it applies in deciding whether public utilities may make power sales at market-based rates. The Commission allows power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, market power in generation and transmission and cannot erect other barriers to entry. In order for a transmission-owning public utility or its affiliate to demonstrate the absence or mitigation of market power, and in particular the absence or mitigation of transmission market power, the transmission-owning public utility must have on file with the Commission an open access transmission tariff for the provision of com-

parable services. The Commission also considers whether there is evidence of affiliate abuse or reciprocal dealing.

If the Commission were called upon to decide whether TVA were entitled to make power sales at market-based rates, I believe that the Commission would be likely to apply these same criteria. I cannot at this juncture, however, in the absence of any factual record (including submissions both from TVA and from other interested parties on, for example, TVA's market power in generation and transmission) conclude whether TVA would or would not be able to meet these criteria.

Question 13. H.R. 2944 directs FERC to approve a transmission surcharge on use of the BPA transmission system for electric sales in the Pacific Northwest. Would it be difficult to fashion this surcharge?

Response. No. Designing a surcharge which would permit BPA to recover shortfalls in power sales revenues from transmission system users would not be difficult. Of course, BPA would be required to fully support its proposed surcharge in order for FERC to carry out its responsibility under H.R. 2944 to accept, reject, or modify the surcharge.

RESPONSES OF HON. JAMES HOECKER TO QUESTIONS FROM HON. VITO FOSSELLA

Question 1. It is my understanding that FERC wants jurisdiction over "retail transmission" which means it will have to deal directly with retail customers. What facilities does FERC have in place to deal with retail customers in terms of servicing their needs, resolving complaints etc. when it now has virtually zero information about local loads and local conditions.

Response. The Federal Power Act places interstate transmission services under the Commission's jurisdiction. Pursuant to Order No. 888, the Commission established open access terms and conditions for all jurisdictional transmission services, including transmission of power that will ultimately be delivered to a retail customer as an unbundled, separate service. However, the Commission also emphasized that Order No. 888 did not affect or encroach upon state authority in such traditional areas as the authority over local service issues, including reliability of local service, authority over utility generation and resource portfolios, and administration of integrated resource planning. Order No. 888, FERC Stats. & Regs. ¶31,036 at 31,782 (1996). As a practical matter, in a retail competition environment, power destined for delivery to retail customers is delivered, on their behalf, to the local distribution company which completes the delivery service under state jurisdiction. In Order No. 888, we established procedures that allow state commissions to request waiver of the standard transmission terms and conditions to the extent necessary to accommodate their retail access programs. To date, this arrangement is working very well. The Commission therefore does not seek or need particular facilities or resources to deal directly with the needs of individual retail consumers of electricity.

Question 2. New York City is unique. It's needs are unique. And to be frank, I am concerned that by enforcing a national standard for reliability, this may result in lowering the standard for some places, such as New York City, since it may prove too costly to reinforce other system's to NYC's level. How would you envision FERC's national reliability standard differing from New York State's reliability standards. In your opinion, would these differences hurt the consumers in New York? If FERC had jurisdiction over reliability of the transmission system, how would FERC coordinate efforts with the states especially during times of system emergencies like storm outages? A concern that I have, and a concern of my city and state, is that FERC might order recovery of the transmission system in its entirety thereby diverting restoration crews away from restoring services to retail customers. This could result in an inefficient use of resources and delayed recovery after a storm.

Response. I believe the Commission's potential role in overseeing the establishment of bulk power reliability organizations and standards does not infringe or compromise in any way the ability of states to ensure the reliability of electric distribution systems on behalf of retail customers. In fact, the system for developing reliability standards under the provisions of H.R. 2944 is very similar to the system currently used. Standards are now, and will continue to be, developed by market participants through regional and national self-regulating organizations. Local and regional protocols are developed and agreed to at the regional level. Reliability protocols that states rely on during emergencies are, and should continue to be, coordinated with regional organizations that represent other parts of the interconnected grid. The primary differences between the current system and the system contained in H.R. 2944 are that the rules would be enforceable and there would be avenues for appeal or review of rules by parties, including states, who believe that the rules

are not providing the best protection of the reliability of their service or that the rules are discriminatory. These kinds of procedural protections would be to the benefit of New York customers as well as others. The State of New York would continue to have the ability to protect the security, adequacy and safety of local service in New York.

FERC does not now have, nor would it have under the provisions of H.R. 2944, a role in emergency responses such as restoration of services after storm outages.

I agree with you that New York City has unique needs. However, its location at the intersection of three ISOs and reliability councils makes it evident that the reliability of bulk power service to the city will depend on effective and uniform maintenance of reliability standards, not just in New York, but across the grid. As the marketplace becomes more diverse and competitive, voluntary industry compliance with reliability standards needs to be buttressed with a limited degree of federal oversight and enforcement power.

Question 3. Does FERC believe it should have the full authority to order the building and siting of new electric transmission lines despite the objections of the host state(s)? Does FERC believe that the language included in Section 105 of the second draft bill, which amends Section 216 of the Federal Power Act would remand this power to FERC and take it away from the states?

Response. H.R. 2944 would not give the Commission authority to order the siting of new transmission lines. This type of land use regulation, *i.e.*, certifying the use of particular land for purposes of transmission facilities, is exercised by the States (although the Commission has similar authority for purposes of certificating natural gas pipelines and non-Federal hydroelectric facilities). As I stated in my testimony, I do not see a current compelling need for the changes specified in section 105 of H.R. 2944 at this time.

I will note that the Commission currently has authority to order the enlargement of transmission capacity in conjunction with an order to provide transmission services under section 211 of the FPA. However, the Commission must terminate an order to enlarge capacity if the transmitting utility has failed, after making a good faith effort, to obtain the necessary approvals or property rights under applicable Federal, State and local laws. The Commission also has imposed on public utilities a similar obligation to enlarge transmission capacity if necessary to meet their open access obligations under Order No. 888. The latter were imposed pursuant to the Commission's authority to remedy undue discrimination under FPA sections 205 and 206.

Section 105 of the second draft bill would provide authority to order construction in a new section 216 of the FPA. Section 216 would require the Commission, before exercising its authority under that section, to refer the matter to a joint board, including one or more representatives from each affected State. I believe that the ability to expand transmission capacity in appropriate ways will be key to competition and efficient wholesale power markets. An effective regional planning effort, which could be accomplished by regional transmission organizations, could complement and assist state siting proceedings.

Question 4: Section 532 of the bill deals with Recovery of Costs—stranded costs per se. As you may know, New York has agreements in place with all relevant parties involved that results in a sharing of these costs. The first batch of these agreements are set to be renegotiated in 2001, and then the following in 2003. Would the language contained in this section or anywhere else in this legislation preempt the agreements NY already has in place or give FERC authority to preempt these agreements? Do you feel that any FERC involvement in any future negotiations would create any obstacles or delays for this process that is already running fairly smoothly in NY?

Response. Section 532 provides that, with regard to any legally enforceable obligation entered into or imposed pursuant to section 210 of the Public Utility Regulatory Policies Act of 1978 prior to the date of enactment of the bill, the FERC "shall promulgate and enforce such regulations as may be required to assure that no utility shall be required directly or indirectly to absorb the costs associated with such purchases from a qualifying facility after the date of the enactment of this Act." I do not read Section 532 or any other section of the bill to preempt the agreements New York already has in place that would result in a sharing of the costs associated with purchases from a qualifying facility. Nor would it give FERC authority to preempt these agreements. Because the bill is silent as to its effect on preexisting agreements such as those you describe, I believe that the bill has no impact on such preexisting agreements.

Further, I do not feel that FERC involvement in any future negotiations would create any obstacles or delays for the process that you indicate is already running fairly smoothly in New York. To the contrary, I believe that the FERC would en-

courage negotiated agreements to address the cost recovery issue. The Commission has expressly encouraged such agreements in the past and has allowed the recovery of a utility's costs incurred pursuant to such an agreement.

I suggest, however, that section 532 be clarified to ensure that utilities may agree to enter into such agreements in the future. As currently written, section 532 could be interpreted to bar a utility from negotiating such an agreement regardless of the benefits of such a settlement.

RESPONSES OF HON. JAMES HOECKER TO QUESTIONS FROM HON. ED BRYANT

Question 1. Would the Tennessee Valley Authority be able to make sales outside the fence at market-based rates?

Response. The Commission has explained in a number of cases in recent years the criteria that it applies in deciding whether public utilities may make power sales at market-based rates. The Commission allows power sales at market-based rates if the seller and its affiliates do not have, or have adequately mitigated, market power in generation and transmission and cannot erect other barriers to entry. In order for a transmission-owning public utility or its affiliate to demonstrate the absence or mitigation of market power, and in particular the absence or mitigation of transmission market power, the transmission-owning public utility must have on file with the Commission an open access transmission tariff for the provision of comparable services. The Commission also considers whether there is evidence of affiliate abuse or reciprocal dealing.

If the Commission were called upon to decide whether TVA were entitled to make power sales at market-based rates, I believe that the Commission would be likely to apply these same criteria. However, I cannot at this juncture, and in the absence of any factual record (including submissions both from TVA and from other interested parties on, for example, TVA's market power in generation and transmission), conclude whether TVA would or would not be able to meet these criteria.

Question 2. What would be the budgetary effect on FERC under a bill such as H.R. 2944?

Response. It is extremely difficult for me to quantify precisely how implementing such a bill will impact the Commission's resources. We are a small agency but one which is working diligently to anticipate many of the fundamental changes occurring in the energy industry. Assuming the Commission were to be authorized to act in the areas specified in H.R. 2944, some increase in our budget request would be likely, especially in the early stages of staffing these efforts. For example, the Commission has traditionally had no responsibility to review or oversee any aspect of the reliability standards process, so we would have to augment our engineering staff to handle these tasks.

Our very preliminary estimates are that $5 to $17 million per year would likely be sufficient to implement the Administration's proposed legislation on electric restructuring. We would expect that the costs may be toward the higher end of this range during initial implementation and then decline over time. H.R. 2944 would cost somewhat less because, for example, it does not contain a provision requiring the Commission to receive and act on State filings on the decision of whether to allow retail choice.

Any estimate I would supply you is necessarily dependent on what array of FERC-related provisions any new legislation might contain; consequently, it is somewhat premature to examine our expected staffing needs and other costs in depth at this time. The Commission will make every effort to minimize the costs of its oversight functions and is currently reengineering its processes to obtain greater productivity from the public's investment.

RESPONSES OF HON. CURT L. HEBERT, JR. TO QUESTIONS FROM HON. JOE BARTON

Question 1. H.R. 2944 clarifies Federal and State jurisdiction, providing for FERC jurisdiction over transmission used for bundled retail sales, and for State jurisdiction over transmission used for bundled retail sales. Is this clarification needed, and does the bill draw the jurisdictional line properly?

Response. H.R. 2944 codifies the jurisdictional split the FERC made in Order No. 888. I find the clarification helpful, in that Congress would endorse FERC's call, but not necessary. Under the current Federal Power Act, the FERC has jurisdiction over transmission that occurs separately from a retail sale and the states have jurisdiction over the transmission portion of a bundled retail sale. I think the bill drew the proper jurisdictional line.

Question 2. In your view, does section 102(a)(2) of H.R. 2944 amend section 212(h) of the Federal Power Act to authorize FERC to order retail wheeling to a consumer served by local distribution facilities in closed states? Is there a need to clarify the definition of "open access" in the legislation?

Response. The current text is confusing. By stating that FERC could order transmission to a customer that purchases from distribution facilities subject to open access, it appears that the authority would apply only to states that introduced competition. In that case, no need exists for the amendment. FERC would control the transmission portion of the unbundled retail sale and the state the distribution.

Moreover, without a definition of open access, and in context of other references in the bill to open access as being in the context of Order No. 888, one could argue that, if the utility is subject to open access, as all IOU's under Order No. 888, FERC may order wheeling even in closed states.

Substituting "retail competition" for "open access" would make the provision most clear.

Question 3. Some charge transmission owners are redesignating transmission facilities as distribution facilities, in order to avoid FERC open access requirements. Have you seen examples of such efforts by utilities? Are these utility efforts being supported by State Public Utility Commissions?

Response. I have read anecdotes of that occurring. I have no evidence that any reclassification has, as its purpose, avoidance of FERC requirements. Indeed, if FERC follows my recommendation on incentives and for-profit RTOs, that kind of evasion would not happen.

Question 4. H.R. 2944 includes an exemption from FERC regulation for small transmission owners. Do you believe this exemption is appropriate? Do you have any comments on the specific exemption provisions in H.R. 2944?

Response. As a believer in incentives, performance based rates and for-profit transco's, I think it inappropriate to exempt small transmission owners from FERC jurisdiction. In a world of command and control, the issue of burden arises. With incentives, however, the industry would focus on economic benefits and opportunities, which should inure to all participants in interstate transmission. I would not favor exemptions.

Question 5. FERC does not regulate transmission systems operated by State and municipal utilities and cooperatives, which are some of the largest systems in the country. State and municipal systems oppose FERC regulation of transmission rates, and want to retain that authority. If State and municipal utility transmission systems continue to remain unregulated could they shift power costs onto their transmission rates? Could they discriminate against competitors?

Response. As I said in my testimony, State and municipal utility systems, and to an extent, cooperatives, must answer to their Legislatures and State governments. Therefore, FERC need not regulate them; under most State constitutions, authority exists to prevent publicly owned systems from engaging in undesirable behavior. In addition, under my vision of truly independent RTOs, State and municipal members could not survive by raising prices for transactions or discriminating.

Question 6. Should FERC regulate transmission not in interstate commerce—such as transmission in non-contiguous States and territories?

Response. No, because these areas would not form part of a national grid, having no connections to the "lower 48" States.

Question 7. NARUC has proposed amending the reliability title of H.R. 2944 to authorize individual States to establish reliability standards. What is your position on this problem? How many States regulate transmission reliability? Would 50 different standards improve reliability? How would 50 different standards affect interstate commerce?

Response. I think that neither FERC nor the States should prescribe reliability standards. As I stated in my testimony, reliability should form one of the factors in performance based rates. I think each plan with each RTO should have its own standards, depending on regional factors. In Mississippi, our Public Service Commission negotiated individual plans for each of our utilities.

Question 8. What is your view of the transmission pricing provisions of the bill introduced by Mr. Sawyer (H.R. 2786)?

Response. I favor incentives and performance based rates, with no guarantees of cost recovery, but with the opportunity to keep profit within a range. I think that, theoretically, we might move to market based rates, but not in the foreseeable future.

Question 9. Some criticize the length of FERC merger proceedings. How long does it take to approve mergers?

Response. I rely on the information in the Chairman's response.

Question 10. H.R. 2944 amends section 203 of the Federal Power Act to expand FERC review of sales of power plants and transmission facilities by State and municipal utilities, cooperatives, and Federal electric utilities. Currently, these sales are not subject to review by FERC, DOJ or the FTC. Is there a need for Federal review of these sales to ensure market power issues are addressed?

Response. No. For state and municipal utilities, the DOJ or FTC would review the sales, if any impact on interstate commerce resulted, unless the state action doctrine applied. Under that judge-made law, the authorities in the States would closely supervise the transaction. If Congress wants to overrule the state action doctrine, I think it better to do so generically, not just in electricity.

For Federal utilities, I would imagine Congress would need to authorize sales, as public funds built them. In that case, Congress would consider all the implications, or Congress could authorize the antitrust agencies to review these issues. They, not FERC have the expertise and the ability to collect information quickly.

Question 11. The Burr bill (H.R. 667) and the Sawyer bill (H.R. 2786) repeal section 203 of the Federal Power Act. What is your view of this proposal?

Response. I favor it, as I testified at the hearing on October 5. The DOJ and FTC, not FERC, have the expertise in antitrust and the experience in mergers. Also, both are accountable for their actions to Congress and the American people.

Question 12. H.R. 2944 allows TVA to sell wholesale power outside the region but provides for FERC regulation of such sales. Could TVA get FERC approval to charge market-based rates for those sales?

Response. Yes, if TVA, as a new entrant in the region, had no market power in the area in which it makes its sales.

Question 13. H.R. 2944 directs FERC to approve a transmission surcharge on the use of the BPA transmission system for electric sales in the Northwest. Would it be difficult to fashion this surcharge?

Response. I disagree with the notion of imposing a transmission surcharge for sales. I dislike subsidies. In any event, FERC does not have the resources to fashion a surcharge that would have to take into account all the interests involved. We would have to balance the interests of transmission customers in proper price signals and the preference customers in low prices. I think we would distort the market. Right now, the best FERC can do in reviewing BPA rates is to take a quick look as to whether the agency will meet its repayment schedule that Congress establishes. I think that FERC would act no better in this instance, either.

RESPONSES OF HON. CURT L. HEBERT, JR. TO QUESTIONS FROM HON. VITO FOSSELLA

Question 1. It is my understanding that FERC wants jurisdiction over "retail transmission" which means it will have to deal directly with retail customers. What facilities does FERC have in place to deal with retail customers in terms of servicing their needs, resolving complaints, etc. when it now has virtually zero information about local loads and local conditions?

Response. FERC does not want jurisdiction over transmission at retail. The Barton bill codifies the jurisdiction FERC asserted in Order No. 888 over interstate transmission of energy when the customer in a state with retail competition purchased from someone besides the local utility. Order No. 888 left the distribution portion in the hands of the State. Therefore, the State, not FERC, will continue to deal with local loads and local conditions in retail sales.

Question 2. New York City is unique. Its power needs are unique. And to be frank, I am concerned that by enforcing a national standard for reliability, this may result in lowering the standard for some places, such as New York City, since it may prove to be too costly to reinforce other systems to NYC's level. How would you envision FERC's national reliability standard differing from New York State's reliability standards? In your opinion, would these differences hurt the consumers in New York? If FERC had jurisdiction over reliability of the transmission system, how would FERC coordinate efforts with the states especially during times of system emergences like storm outages? A concern I have, and a concern of my city and state, is that FERC might order recovery of the transmission system in its entirety thereby diverting restoration crews away from restoring services to retail consumers. This could result in an inefficient use of resources and delay recovery after a storm.

Response. I oppose FERC having authority to establish reliability standards. I also think that the current system, involving private regional reliability councils establishing the standards needs reform. I favor injecting reliability standards in the performance based rate plans I advocate for utilities. In particular, each plan for each Regional Transmission Organization would contain a target for reliable per-

formance. I envision interested parties negotiating the issue, along with the other factors in the plan for presentation to FERC. Each RTOs earnings would rise or fall on how well it does. Therefore, in the case of storms, rather than have FERC order deployment of crews, the RTO would find it in its economic interest to do the best job it could.

In any event, it is my belief that even my colleagues favoring a FERC role would not necessarily establish the same standard for the whole Nation or fashion maximum, rather than minimum standards. I also do not envision FERC directing crews in storms, even if we received authority over reliability.

Question 3. Does FERC believe it should have the full authority over the building and siting of new electric transmission lines despite the objections of the host state(s)? Does FERC believe that the language in Section 105 of the second bill draft, which amends Section 216 of the Federal Power Act would remand this power to FERC and take it away from the states?

Response. I oppose giving FERC authority to approve building and siting of transmission facilities. I think FERC could better give economic incentives for transmission expansion and upgrade. We should reform our pricing policy that looks at cost recovery, rather than economic value and efficiency. Several bills, including the Barton bill, contain provisions for incentive pricing. I think in that way, FERC would encourage a more efficient transmission system through the market.

I think Section 105 does not take away siting authority from the States. That section gives utilities the opportunity to reverse a FERC order requiring expansion, if the necessary State or local agencies deny permits.

Question 4. Section 532 of the bill deals with Recovery of Costs—stranded costs per se. As you may know, New York has agreements in place with all relevant parties involved that result[] in a sharing of these costs. The first batch of these agreements [is] set to be renegotiated in 2001, and then the following in 2003. Would the language contained in this section or anywhere else in this legislation preempt the agreements NY already has in place or give FERC authority to preempt these agreements? Do you feel that any FERC involvement in any future negotiations would create any obstacles or delays in this process that is already running fairly smoothly in NY?

Response. Section 532 states that any FERC rule would apply prospectively. FERC has refused to compel renegotiation of PURPA contracts and, in fact, preempted states, such as California, from abrogating existing PURPA contracts.

As for FERC's role in renegotiations, it would depend on the wishes of the State. For example, last fall, New York, through Chair Maureen Helmer of the Public Service Commission, asked for FERC's help in renegotiating the PURPA contracts of New York State Electric and Gas Company, an upstate utility. Eventually, the New York Commission brought the parties together, without FERC's involvement.

RESPONSES OF HON. VICKEY A. BAILEY TO QUESTIONS FROM HON. JOE BARTON

Question 1. H.R. 2944 clarifies Federal and State jurisdiction, providing for FERC jurisdiction over transmission used for unbundled retail sales, and for State jurisdiction over transmission used for bundled retail sales. Is this clarification needed, and does the bill draw the jurisdictional line properly?

Response. I think this clarification is useful. The clarifying language adopts, for the most part, the jurisdictional dividing lines adopted by the Commission in its Order No. 888 rulemaking; those lines, for the most part, have been accepted by industry participants and state regulatory commission. I believe it is important, whenever possible, to eliminate jurisdictional turf battles and protracted court disputes over ambiguous congressional delegations, in order to ensure that the benefits of increased competition flow through to consumers as quickly and comprehensively as possible.

In light of recent court litigation on the subject of comparability of service, cited in Chairman Hoecker's response, I have no objection to an additional clarification that would further codify existing Commission policy. That policy, based on the Commission's authority to protect against undue discrimination or preference in the provision of transmission service, requires that a transmission-owning utility offer transmission service to others that is comparable to (i.e., no worse than) the service it provides to itself.

Question 2. In your view, does section 102(a)(2) of H.R. 2944 amend section 212(h) of the Federal Power Act to authorize FERC to order retail wheeling to a consumer served by local distribution facilities in closed States? Is there a need to clarify the definition of "open access" in the legislation?

Response. I recall this question coming up during the question and answer session of the FERC Commissioner panel of the October 5 hearing on H.R. 2944. The explanation we received from the Committee is that section 102(a)(2) does not authorize the Commission to order wheeling to retail customers in "closed" states (that have not adopted retail competition). I am fine with this explanation. If, however, there is some perception of ambiguity in the reference to "local distribution facilities that are subject to open access," I have no objection to a clarification that explains that the Commission's authority to order retail wheeling is confined to consumers in "open" states that have adopted retail competition.

Question 3. Some charge transmission owners are redesignating transmission facilities as distribution facilities, in order to avoid FERC open access requirements. Have you seen examples of such efforts by utilities? Are these utility efforts being supported by State public utility commissions?

Response. I am aware that some utilities are redesignating transmission facilities as distribution facilities. The Commission occasionally reviews such a redesignation in the context of utility filings that reflect the rate consequences of such a redesignation; in these circumstances, the Commission is very deferential of the state commission's characterization of transmission and distribution facilities. Such deference to state designations of transmission and distribution facilities is contemplated in Order No. 888 (which adopts a 7-factor test for analysis).

Obviously, the redesignation of a facility from transmission to distribution acts to remove that facility from aspects of Commission regulation. But I am not in a position to assess the motivation of any such T/D redesignation, or to suggest that any such undertaking is one merely to evade Commission jurisdiction (such as a direction to provide open access, non-discriminatory service).

Question 4. H.R. 2944 includes an exemption from FERC regulation for small transmission owners. Do you believe this exemption is appropriate? Do you have any comments on the specific exemption provisions in H.R. 2944?

Response. I have no problem with the exemption provisions in H.R. 2944. They reflect, for the most part, the Commission's existing practice. Specifically, the Commission already waives the requirements of Order Nos. 888 (to provide open access transmission service) and 889 (to participate in an Internet-based transmission information system and to separate transmission from wholesale merchant functions) for transmission-owning utilities that are small and/or own limited and discrete transmission facilities.

Question 5. FERC does not regulate transmission systems operated by State and municipal utilities and cooperatives, which are some of the largest systems in the country. State and municipal utilities oppose FERC regulation of transmission rates, and want to retain that authority. If State and municipal utility transmission systems continue to be unregulated could they shift power cost onto their transmission rates? Could they discriminate against competitors?

Response. I am in agreement with Chairman Hoecker's response to this question. I add that a number of government-owned and cooperative-owned utilities already have consented to follow the open access requirements applicable to transmission-owning public utilities subject to Commission regulation, in order for themselves to be eligible for "reciprocal" open access service. In addition, an increasing number of cooperative-owned utilities are buying out their debt to the U.S. government (through the Rural Utilities Service of the U.S. Department of Agriculture) and are thus voluntarily acceding to Commission jurisdiction over their rates and terms of service.

Question 6. Should FERC regulate transmission that is not in interstate commerce—such as transmission in noncontiguous States and territories?

Response. A series of court cases through the decades have established that all transmission in the continental (lower 48 states of the) United States—with the exception of transmission within the Electric Reliability Council of Texas—is in interstate commerce. I am in agreement with Chairman Hoecker's response to this question as it relates to the activities of ERCOT utilities.

Question 7. NARUC proposed amending the reliability title of H.R. 2944 to authorize individual States to establish reliability standards. What is your position on this proposal? How many States regulate transmission reliability? Would 50 different reliability standards improve reliability? How would 50 different standards affect interstate commerce?

Response. As a general matter, I much prefer fewer layers of regulatory review rather than more. Nevertheless, I have no objection to legislative language of the type found in section 201 of H.R. 2944 that would clarify the authority of states and local authorities to ensure the reliability of local distribution facilities. As electricity markets become increasingly competitive, close cooperation with state and local regulatory authorities with oversight over the reliability of local distribution facilities

become imperative. Well-publicized power outages in the last year (such as in San Francisco, New York City, and Chicago), due to isolated inadequacies in local distribution infrastructure, suggest that federal regulatory oversight, in itself, cannot assure the continued reliability of local service. Moreover, I am appreciative of limiting language, such as that found in revised section 217(n) of the FPA, that acts to ensure that any such exercise of state or local authority cannot "unreasonably impai[r] the reliability of the bulk power system."

Question 8. What is your view of the transmission pricing provisions of the bill introduced by Mr. Sawyer (H.R. 2786)?

Response. Among the many transmission pricing provisions of Mr. Sawyer's bill, my principle interest lies in those that would offer incentives to transmitting utilities for engaging in various types of Commission-favored activities. I support the use of incentives to promote—rather than compel—participation in regional transmission organizations. As I explain in my written testimony, I favor the use of incentives that encourage utility innovation and individual design, rather than federal legislation that compels utility RTO filings and participation by a date certain. I also favor incentives that act to promote reliable and efficient transmission operations and that encourage investment in and expansion of transmission facilities.

As Chairman Hoecker explains, however, the Commission already retains the flexibility under the Federal Power Act, as currently written, to pursue much or all of these behavior-based policy objectives.

Question 9. Some criticize the length of FERC merger proceedings. How long does it take FERC to approve mergers?

Response. Chairman Hoecker's response provides the raw data. The vast majority of the merger applications the Commission receives are processed in a timely manner. Nevertheless, I fail to understand why the Commission cannot process *all* merger applications in a timely manner (say, 150, 180 or 240 days at most) that will provide the type of predictability and uniformity necessary to allow utilities to restructure themselves in a manner that, in their judgment, is best able to respond and adapt to the same competitive forces that the Commission is attempting to promote.

The trend toward utility consolidation is accelerating. The Commission is starting to receive a number of merger applications involving larger utility applicants. These applications likely will attract numerous interventions and vigorously-argued calls for extended evidentiary hearings, for numerous "pro-competitive" conditions to approval, or for outright rejection. My understanding is that financial markets and developing business strategies cannot await over a year of uncertainty while the Commission parses through the various options.

Question 10. H.R. 2944 amends section 203 of the Federal Power Act to expand FERC review of sales of power plants and transmission facilities by State and municipal utilities, cooperatives, and Federal electric utilities. Currently, those sales are not subject to review by FERC, DOJ, or FTC. Is there a need for Federal review of these sales to ensure market power issues are addressed?

Response. Frankly, I do not perceive a gap in regulatory oversight over utility asset sales that requires an expansion of federal jurisdiction. Market power issues currently are being addressed by the Commission, in its continuing assessment of: (1) the utility mergers and asset sales over which it currently does have authority to review; and (2) utility requests to sell power at wholesale at negotiated, market-based rates. Moreover, the Commission is actively monitoring the competitive operation of wholesale power markets. If the Commission detects the presence or exercise of market power, it retains the authority to adopt utility-specific corrective action. (Similar market monitoring and enforcement activity currently is undertaken in regional markets by the regional transmission institutions that the Commission already has approved.)

Question 11. The Burr bill (H.R. 667) and the Sawyer bill (H.R. 2786) repeal section 203 of the Federal Power Act. What is your view of this proposal?

Response. To date, I have refrained from advocating the outright repeal of section 203 of the Federal Power Act. I agree with Chairman Hoecker to the extent he responds that the Commission retains a unique and vital regulatory role under section 203—but *only* if that role is exercised in a timely manner (say, no more than 150-240 days). If Commission merger review extends beyond that limited time frame, I believe Commission merger review becomes counter-productive, as it would inhibit the ability of utilities to take advantage of competitive opportunities and to develop pro-competitive business strategies.

Question 12. H.R. 2944 allows TVA to sell wholesale power outside the region but provides for FERC regulation of such sales. Could TVA get FERC approval to charge market-based rates for these sales?

Response. I have nothing to add to Chairman Hoecker's response to this question.

Question 13. H.R. 2944 directs FERC to approve a transmission surcharge on use of the BPA transmission system for electric sales in the Pacific Northwest. Would it be difficult to fashion this surcharge?

Response. I have nothing to add to Chairman Hoecker's response to this question.

RESPONSES OF HON. WILLIAM L. MASSEY TO QUESTIONS FROM HON. JOE BARTON

Question 1. H.R. 2944 clarifies Federal and State jurisdiction, providing for FERC jurisdiction over transmission used for unbundled retail sales, and for State jurisdiction over transmission used for bundled retail sales. Is this clarification needed, and does the bill draw the jurisdictional line properly?

Response. I believe that a clarification of Federal and State jurisdiction over the uses of transmission is necessary, but I fear that the one that is proposed in H.R. 2944 will lead to a further balkanization of the interstate grid. As Chairman Hoecker points out, the historical regulatory practice adopted in Order No. 888 of treating native load uses of transmission differently from all other uses of transmission makes less sense in a competitive wholesale market environment. Efficient electricity markets require that all grid users be subject to the same rules. Different transmission rules set by individual states will result in discriminatory access and a balkanization of the markets that are now developing. My preference would be to broaden the Commission's jurisdiction to include all uses of transmission, whether bundled or unbundled, so as to ensure that the Nation's transmission grid will support efficient electricity commerce.

Question 2. In your view, does section 102(a)(2) of H.R. 2944 amend section 212(h) of the Federal Power Act to authorize FERC to order retail wheeling to a consumer served by local distribution facilities in closed States? Is there a need to clarify the definition of "open access" in the legislation?

Response. I endorse Chairman Hoecker's response to this question.

Question 3. Some charge transmission owners are redesignating transmission facilities as distribution facilities in order to avoid FERC open access requirements. Have you seen examples of such efforts by utilities? Are these utility efforts being supported by State public utility commissions?

Response. I endorse Chairman Hoecker's response to this question. I would also make two additional points. First, I would be deeply concerned if the Commission's review of reclassification proposals indicated that such reclassifications were being accomplished to avoid Commission jurisdiction and open access requirements. Second, I would like to point out that, in addition to impairing the availability of open access transmission service, strategic reclassifications can result in the addition of distribution charges on certain generation facilities and thereby make those assets, or service from those assets, more costly than the transmission provider's own generation assets or services.

Question 4. H.R. 2944 includes an exemption from FERC regulation for small transmission owners. Do you believe this exemption is appropriate? Do you have any comments on the specific exemption provisions in H.R. 2944?

Response. I endorse Chairman Hoecker's response to this question.

Question 5. FERC does not regulate transmission systems operated by State and municipal utilities and cooperatives, which are some of the largest systems in the country. State and municipal utilities oppose FERC regulation of transmission rates, and want to retain that authority. If State and municipal utility transmission systems continue to be unregulated could they shift power costs onto their transmission rates? Could they discriminate against competitors?

Response. I endorse Chairman Hoecker's response to this question. I believe that all transmission in interstate commerce, regardless of ownership, should be directly subject to the Commission's open access policies. I would also like to mention that under Order No. 888's reciprocity provisions, a number of non-jurisdictional transmission providers have filed open access tariffs with terms and conditions that are consistent with Order No. 888.

Question 6. Should FERC regulate transmission that is not in interstate commerce—such as transmission in noncontiguous States and territories?

Response. I endorse Chairman Hoecker's response to this question.

Question 7. NARUC proposed amending the reliability title of H.R. 2944 to authorize individual States to establish reliability standards. What is your position on this proposal? How many States regulate transmission reliability? Would 50 different reliability standards improve reliability? How would 50 different standards affect interstate commerce?

Response. I endorse Chairman Hoecker's response to this question. I would add as a caveat that, because effective electricity markets do not respect state bound-

aries, we should strive for as much regional or national uniformity in reliability standards as possible.

Question 8. What is your view of the transmission pricing provisions of the bill introduced by Mr. Sawyer (H.R. 2786)?

Response. I endorse Chairman Hoecker's response to this question in most respects. I would like to be clear, however, that I do not favor financial bonuses or incentives to entice transmission owners to participate in RTOs. As I discussed in my testimony, such bonuses are not free. They are paid for by transmission system users, and ultimately by consumers, in the form of higher electricity rates. I do, however, favor performance-based incentives where clearly defined performance standards are met or exceeded by transmission operators.

Question 9. Some criticize the length of FERC merger proceedings. How long does it take FERC to approve mergers?

Response. I endorse Chairman Hoecker's response to this question.

Question 10. H.R. 2944 amends section 203 of the Federal Power Act to expand FERC review of sales of power plants and transmission facilities by State and municipal utilities, cooperatives, and federal electric utilities. Currently, those sales are not subject to review by FERC, DOJ, or FTC. Is there a need for federal review of these sales to ensure market power issues are addressed?

Response. I endorse Chairman Hoecker's response to this question.

Question 11. The Burr bill (H.R. 67) and the Sawyer bill (H.R. 2786) repeal section 203 of the Federal Power Act. What is your view of this proposal?

Response. I endorse Chairman Hoecker's response to this question. I feel strongly that repeal of the Commission's merger authority is not in the public interest, and particularly not during the massive industry consolidation now underway.

Question 12. H.R. 2944 allows TVA to sell wholesale power outside the region but provides for FERC regulation of such sales. Could TVA get FERC approval to charge market-based rates for these sales?

Response. I endorse Chairman Hoecker's response to this question.

Question 13. H.R. 2944 directs FERC to approve a transmission surcharge on use of the BPA transmission system for electric sales in the Pacific Northwest. Would it be difficult to fashion this surcharge?

Response. I endorse Chairman Hoecker's response to this question.

RESPONSES OF HON. LINDA K. BREATHITT TO QUESTIONS FROM HON. JOE BARTON

Question 1. H.R. 2944 clarifies Federal and State jurisdiction, providing for FERC jurisdiction over transmission used for unbundled retail sales, and for State jurisdiction over transmission used for bundled retail sales. Is this clarification needed, and does the bill draw the jurisdictional line properly?

Response. The clarification given in H.R. 2944 pertaining to Federal and State jurisdiction over transmission is consistent with the findings made by the Commission in Order No. 888, which was issued in 1996. In that ruling, the Commission determined that it has jurisdiction over unbundled retail transmission, and that States have jurisdiction over bundled retail transmission. Therefore, it is appropriate for Congress to amend the Federal Power Act (FPA) as proposed in section 101(b)(1) of H.R. 2944. However, as Chairman Hoecker contends in his response to this question, if such an amendment is made, additional legislative language is necessary to ensure the Commission's ability to require non-discrimination in the uses of the transmission grid. Chairman Hoecker has suggested, both in his written testimony before the Subcommittee and in his response to this question, specific language to be added at the end of FPA Section 201(a), as modified by H.R. 2944. I concur with Chairman Hoecker that such additional language would be necessary.

Question 2. In your view, does section 102(a)(2) of H.R. 2944 amend section 212(h) of the Federal Power Act to authorize FERC to order retail wheeling to a consumer served by local distribution facilities in closed States? Is there a need to clarify the definition of "open access" in the legislation?

Response. Section 102(a)(2) amends Section 212(h) of the FPA to clarify FERC authority to order transmission of electric energy to retail electric consumers served by local distribution facilities subject to open access. It is clear to me that, as drafted, section 102(a)(2) would apply only to those States which have enacted retail open access. In other words, FERC would have authority to order retail wheeling only in "open" states, not in "closed" states. As far as the definition of "open access" used in the legislation, I concur with Chairman Hoecker that transmission open access should be given the meaning the Commission gave it in Order No. 888.

Question 3. Some charge transmission owners are redesignating transmission facilities as distribution facilities in order to avoid FERC open access requirements.

Have you seen examples of such efforts by utilities? Are these utility efforts being supported by State public utility commissions?

Response. The issue of transmission/distribution reclassification is one that concerns me, and I might add is a relatively new area brought about by retail open access plans. As Chairman Hoecker mentions in his response, several utilities have filed with the Commission proposals to classify certain facilities as either transmission or distribution. Some of the recent filings propose substantial reclassifications of transmission facilities as distribution facilities. As these cases are pending before the Commission, it would be inappropriate to discuss them. However, I believe these are important cases that deserve careful attention by the Commission.

Question 4. H.R. 2944 includes an exemption from FERC regulation for small transmission owners. Do you believe this exemption is appropriate? Do you have any comments on the specific exemption provisions in H.R. 2944?

Response. I concur with Chairman Hoecker's response to this question.

Question 5. FERC does not regulate transmission systems operated by State and municipal utilities and cooperatives, which are some of the largest systems in the country. State and municipal utilities oppose FERC regulation of transmission rates, and want to retain that authority. If State and municipal utility transmission systems continue to be unregulated could they shift power costs onto their transmission rates? Could they discriminate against competitors?

Response. In my written testimony before the Subcommittee I contend that, despite the Commission's diligent efforts to create an open, non-discriminatory transmission system, certain impediments to full open access remain. One such impediment is that a significant portion of the Nation's transmission grid is owned and operated by utilities not subject to Commission open access requirements. I support section 102(b) of H.R. 2944, which amends the definition of "public utility" in the FPA to include transmitting utilities and provides FERC authority over the transmission systems of State and municipal utilities and rural electric cooperatives. I believe this provision would result in a more cohesive transmission grid and will greatly facilitate open transmission access. I believe the potential exists for any regulated or unregulated transmission system to shift costs inappropriately and discriminate against competitors. However, I prefer to believe that discriminatory practices are the exception rather than the rule. Nevertheless, it is important that FERC have jurisdiction to regulate the transmission rates, terms, and conditions of these utilities.

Question 6. Should FERC regulate transmission that is not in interstate commerce—such as transmission in noncontiguous States and territories?

Response. I concur with Chairman Hoecker's response to this question. In particular, I believe the success of open, non-discriminatory transmission access depends on the consistent application of transmission rules across the interconnected grid. To this end, I reiterate Chairman Hoecker's request that Congress not deny the Commission the limited authority it now has under section 211 of the FPA to order transmission by utilities within ERCOT.

Question 7. NARUC proposed amending the reliability title of H.R. 2944 to authorize individual States to establish reliability standards. What is your position on this proposal? How many States regulate transmission reliability? Would 50 different reliability standards improve reliability? How would 50 different standards affect interstate commerce?

Response. I concur with Chairman Hoecker's response to this question. In particular, I support the reliability provisions in Title II of H.R. 2944, which, among other things, adds a new section 217(n) to the FPA preserving State and local authority to ensure the reliability of local distribution facilities within the State, except where the exercise of such authority unreasonably impairs the reliability of the bulk power system. As Chairman Hoecker states, H.R. 2944, as drafted, would not prevent States from acting to protect the reliability of local distribution, as long as they do so in a manner that is consistent with the rules that apply across the transmission system.

Question 8. What is your view of the transmission pricing provisions of the bill introduced by Mr. Sawyer (H.R. 2786)?

Response. I concur with Chairman Hoecker's response to this question.

Question 9. Some criticize the length of FERC merger proceedings. How long does it take FERC to approve mergers?

Response. I believe that such criticism is unwarranted. As I indicate in my written testimony, the Commission has shown repeatedly that it processes merger applications within the 150-day period prescribed in our 1996 Merger Policy Statement. As Chairman Hoecker notes in his response to this question, of the 24 merger applications the Commission has acted on since 1996, only 3 were set for hearing. The

remaining applications were consistently processed within the prescribed time period.

Question 10. H.R. 2944 amends section 203 of the Federal Power Act to expand FERC review of sales of power plants and transmission facilities by State and municipal utilities, cooperatives, and federal electric utilities. Currently, those sales are not subject to review by FERC, DOJ, or FTC. Is there a need for federal review of these sales to ensure market power issues are addressed?

Response. As stated in my written testimony, I support the provisions of section 401 of H.R. 2944, which authorizes the Commission to review proposed mergers and disposition of facilities of all electric utilities and transmitting utilities, including State and municipal utilities, most rural electric cooperatives, and Federal electric utilities. Given the changing nature of the electric industry and in order to protect the public interest, I believe it is essential that the Commission continue to evaluate public utility mergers and that the scope of our merger authority be extended as proposed in section 401 of the bill.

Question 11. The Burr bill (H.R. 67) and the Sawyer bill (H.R. 2786) repeal section 203 of the Federal Power Act. What is your view of this proposal?

Response. I join Chairman Hoecker in strongly opposing repeal of section 203 of the FPA. I believe the Commission's authority to review public utility mergers is vital to the public interest. Furthermore, I am convinced that the Commission is uniquely situated and eminently qualified to assess a proposed merger's effects on competition, rates and regulation. Given the Commission's special expertise and knowledge of the electric industry, I believe that retention of the Commission's merger authority is absolutely necessary.

Question 12. H.R. 2944 allows TVA to sell wholesale power outside the region but provides for FERC regulation of such sales. Could TVA get FERC approval to charge market-based rates for these sales?

Response. I concur with Chairman Hoecker's response to this question.

Question 13. H.R. 2944 directs FERC to approve a transmission surcharge on use of the BPA transmission system for electric sales in the Pacific Northwest. Would it be difficult to fashion this surcharge?

Response. I concur with Chairman Hoecker's response to this question.

RESPONSES OF MARSHA H. SMITH, COMMISSIONER, IDAHO PUBLIC UTILITIES COMMISSION, ON BEHALF OF THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS TO QUESTIONS FROM HON. JOE BARTON

Question 1. The Administration proposes a public benefits fund financed by a new $3 billion tax on electric generation. This proposal is based on a theory States will slash public benefits programs as they open retail electric markets. 24 States have opened their retail markets. How many slashed their public benefits programs? How many strengthened their programs? Is a Federal public benefits fund needed if States maintain public benefits programs?

Answer: NARUC is currently in the process of producing a database to track the various policy elements found in each State restructuring plan. This database is not yet completed to the extent that would allow us to give a definitive answer. However, the initial research we have done appears to show mixed results depending upon the specific program in a particular State. Some States have increased some programs and decreased others, while other States made no changes to the way they handled public benefits programs.

While we expect States to continue playing an important role in maintaining public benefits, NARUC believes there is a Federal role as well. Our policy on public benefits in restructured utility markets supports the inclusion in Federal legislation of "workable mechanisms to support State and utility public benefits programs." In developing these mechanisms, we believe that Congress should focus its attention on the following goals:

- A Federal-State partnership, building upon state and utility expertise in designing and implementing electric service and public purpose programs, and leaving the greatest possible degree of flexibility and regulatory oversight to individual States;
- Such programs may be designed, supported, and delivered through the nation's electric system, using broad-based, competitively-neutral funding mechanisms, subject to regulatory oversight; and
- Federal support should be made available to assist and encourage the states to develop and implement public purpose programs that meet the needs of the States and the nation.

Further, we believe that there is a National interest in diversity of generation resources, including necessary and appropriate public interest research and development, to support a continuing Federal role in this area during and after the restructuring process.

Question 2. Under the Administration bill, only certain public benefits programs are eligible for Federal matching grants—low income assistance, energy conservation, consumer education, research and development programs that provide environmental benefits, and rural assistance. Should Congress limit the ability of States to fund public benefits programs?

Answer: NARUC's position, independent of the Administration's specific proposal, is that Congress should not limit the ability of States to fund public benefits programs by either restricting the mechanisms used to support such programs or limiting their scope.

Question 3. H.R. 2944 clarifies State authority to impose public purpose charges to fund programs of their own design, even if no State jurisdictional facility (such as distribution) is used. Do you believe this approach is preferable to a Federal public benefits fund?

Answer: NARUC strongly supports legislation that removes any doubt that States can establish funding mechanisms for public benefit programs. We believe that there is also a Federal role in this area, consistent with the principles described in our answer to Question 1 above.

Question 4. The Pallone bill (H.R. 2569) includes a Federal public benefits fund different from the Administration's proposal. The bill sets different limits for State public benefits programs, imposes a new distribution tax instead of a new generation tax, and is twice as large ($6 billion instead of $3 billion). What is NARUCs position on the public benefits provisions of H. R. 2569?

Answer: NARUC has taken no position on the size of any Federal public benefits program that restructuring legislation would establish. Again, as our answer to Question 1 states, we do believe that there is a Federal role in this area that goes beyond the removal of barriers to State programs.

Question 5. Some witnesses support including market power provisions in electricity legislation, authorizing FERC to order divestiture if it determines an electric supplier has generation market power. Does NARUC support these proposals? Do States have authority to address generation marketpower?

Answer: First of all, Congress should not preempt State jurisdiction to address market power issues. We believe that divestiture is not the only option available to mitigate market power in the generation market. State regulators must have at their disposal a continuum of options for the mitigation of market power, and accordingly, we urge Congress to preserve State flexibility to use these options as needed. Legislation should clarify the authority of States to use accounting conventions and codes of conduct, which may be sufficient safeguards in some cases. Legislation should clarify the authority of the States to require and police the separation of utility and non-utility, and monopoly and competitive businesses, and to impose affiliate transaction and other rules to assure that electric customers do not subsidize non-utility ventures. Legislation should clarify that States have clear authority to require the formation of appropriate state and regional institutions where necessary to ensure a competitive electricity market. As market power abuse may require the application of well-tailored structural solutions, legislation should clarify that the States are not restricted in their authority to require divestiture where appropriate and necessary. Additionally, Congress should also clarify that States have the ultimate and meaningful authority to ensure effective retail markets and should eliminate any barriers to the exercise of that authority by the States.

Second, concerning the scope of FERC's authority to address market power issues, Congress may well conclude that FERC should have a similar array of options to apply in specific cases. We believe that any new authority granted the Commission to address issues within its jurisdiction should complement the work of the States and such other Federal agencies as the Federal Trade Commission and Department of Justice and not preempt or restrict actions taken at the State level.

Question 6. How many of the 24 States that opened their retail markets addressed generation market power issues? Some States—Texas, California, New York, and the New England States—included generation market power provisions. Others—New Jersey and Pennsylvania—did not.

Answer: Our preliminary analysis of State restructuring policies indicates that many States have provided their regulatory commissions with the array of options described in our answer to Question 5. While we haven't been able to conduct an exhaustive analysis of State restructuring legislation since we received the Subcommittee's questions, we can report that States that have restructured retail markets have provided their regulators with the authority to order divestiture of gen-

eration facilities directly or as a condition for the recovery of stranded costs (Maine, New Jersey, Nevada, Delaware, Arkansas, Massachusetts, Connecticut), the authority to require separate subsidiaries for regulated and non-regulated businesses (Nevada, New Jersey, Rhode Island, Connecticut, New Hampshire, Ohio, Virginia, Maryland, Maine), the authority to require functional separation of competitive and regulated businesses (i.e. the model adopted by FERC in Order No. 888) (Illinois, New Jersey, Arkansas), and the authority to revoke subsidiary licenses for market power abuses (New Jersey).

Question 7. The Administration bill authorizes FERC to provide backup market power remedies for retail markets at the request of States lack of authority to remedy market power. Do States lack authority to remedy marketpower issues?

Answer: As our answers to Questions 5 and 6 indicate, States do not lack authority to remedy market power abuses that are within their jurisdictional authority under the Federal Power Act. Any legislation Congress considers that affects the allocation of jurisdiction must not restrict the ability of States to monitor market behavior and impose remedies necessary to protect consumers from market power abuses.

Question 8. H.R. 2944 clarifies Federal and State jurisdiction, providing for FERC jurisdiction over transmission used for unbundled retail sales, and for State jurisdiction over transmission used for bundled retail sales. Is this clarification needed, and does the bill draw the jurisdictional line properly?

Answer: NARUC believes clarification of Federal and State jurisdiction is needed. However, the bill does not draw the jurisdictional line properly. We support a jurisdictional division based upon the bright line distinction between wholesale and retail services: FERC would exercise jurisdiction to regulate wholesale power transactions, including the transmission services necessary to complete such transactions, and States would exercise jurisdiction to regulate retail power transactions, including the transmission and distribution services necessary to complete such transactions. Jurisdiction, including ratemaking authority, should not shift based upon State decisions to allow customer choice. Accordingly, NARUC does not support the bill's allocation to FERC of regulatory authority over unbundled retail sales.

Similarly, we oppose other proposals that would be even more preemptive of State authority to regulate services provided retail customers, such as the proposals by Americans for Affordable Energy (AAE) and FERC Chairman Hoecker that would give FERC exclusive jurisdiction to regulate all retail transmission services, whether bundled or unbundled. Members of Congress should understand what these proposals ask it to do: provide a distant FERC *exclusive* authority to regulate prices and conditions of service provided by facilities that were planned and constructed to serve retail customers, that have been paid for by retail customers, and that criss-cross the fields, towns, forests and waterways owned by or adjacent to retail customers.

Our proposal (retail authority to the States, wholesale to the FERC) is not a formula for chaos, or balkanization of the grid, or a crazy quilt. Rather, the situation described in Elizabeth Moler's testimony for AAE (i.e. the difference between transmission service in Virginia and West Virginia) is directly attributable to the decision FERC made in Order No. 888 to assert jurisdiction over unbundled retail transmission services. Had FERC not done so, regulatory jurisdiction would now be uniform in Virginia and West Virginia—both State commissions would regulate transmission services provided retail customers whether bundled (West Virginia) or unbundled (Virginia).

Nor is it unusual for State and Federal regulators to share regulatory authority over facilities used for services provided in both jurisdictions. Indeed, this was the very state of affairs in the electricity industry beginning in 1935 when Congress first adopted the wholesale/retail distinction. Similar situations occur in the telecommunications industry where plant and equipment is used for both local and long-distance services. In sum, Congress should clarify the Federal Power Act to ensure that services provided to retail customers remain subject to State authority.

Question 9. Some charge transmission owners are redesignating transmission facilities as distribution facilities to avoid FERC open access requirements. Have you seen examples of such efforts? Are any such utility efforts being supported by State public utility commissions?

Answer: NARUC is aware of recent reports claiming that transmission owners are using the "seven-factor test" adopted by FERC in Order No. 888 to "refunctionalize" their facilities. We are also aware of suggestions that this process is resulting in the conversion of facilities from Federally-regulated transmission to State-regulated distribution. Finally, we understand that the implementation of the seven-factor test is occurring in State regulatory proceedings where State commissions are making findings that are then implemented through FERC's Order No. 888 open-access tar-

iffs. However, while we have not had time to conduct an exhaustive evaluation of State decisionmaking in this area, we can report the following:

The Illinois Commerce Commission conducted extensive time consuming proceedings to apply the seven-factor test to its jurisdictional utilities. As Order No. 888 requires, the work conducted by the Illinois staff involved detailed analyses of diagrams and descriptions of the facilities comprising each utility's power delivery system. Application of the seven-factor test in Illinois resulted in some significant reclassification of facilities from transmission to distribution—up to 40% in the case of Commonwealth Edison. The Illinois staff is convinced that their Commission applied the test as FERC intended in Order No. 888, and that if there is a problem, it is attributable to the test itself.

Similarly, the New York Public Service Commission conducted a classification proceeding to develop rules that categorize utility facilities consistently with FERC's Order No. 888 policies, focussing its attention on cost allocation and revenue impact issues, i.e. how the application of FERC's policies, supplemented with additional technical factors tailored to local conditions, would affect consumer rates. Importantly, while the rules developed in this proceeding have not been fully implemented, the New York commission undertook its analysis with the goal of supporting competitive markets in the State, not to restrict access or deny service.

Some observations on the issue of refunctionalization:

- First, NARUC did not support the adoption of the seven-factor test by Order No. 888. We believed at the time that contrary to the Supreme Court's long-standing admonition that there be a "bright-line" between State and Federal jurisdiction, the "seven-factor test" would lead to case-by-case, power line-by-power line jurisdictional determinations based upon weighing and reweighing of the factors. In other words, it was our view that a multifactor test could only lead to differing outcomes in different cases. It would appear that in this respect, Order No. 888 is operating exactly as FERC intended: State commissions are making case-by-case determinations in the first instance based upon application of the seven factors, and the results then go to the Federal level to be implemented via tariff.
- Second, from the perspective of retail competition, it is not clear that refunctionalization (to the extent it's occurring) is necessarily being undertaken to avoid open-access requirements as much as it is to shift costs from the Federal to State jurisdiction. In open access States, transmission owners that also provide distribution services (i.e. the vertically integrated utilities formerly providing bundled services) must provide open access service to retail customers regardless of the character (transmission or distribution) of the specific facilities used to deliver the power. Accordingly, if the entire retail transaction is subject to one jurisdictional authority at the State level (covering transmission and distribution services), refunctionalization can provide no escape from open access requirements.
- Third, our proposal to allocate jurisdiction based on how facilities are used rather than through case-by-case application of seven technical factors restores the bright line and limits the opportunity to shift facilities from one side of the jurisdictional line to the other. Clearly, an allocation of jurisdiction based upon wholesale (FERC) and retail (State) service avoids the case-by-case problems of the seven-factor test while preserving the categorization of facilities as State, Federal or joint that has existed for decades.

Question 10. Should FERC regulate transmission that is not in interstate commerce—such as transmission in noncontiguous States and territories?

Answer: As a preliminary matter, the extension of FERC authority to reach transmission services that are not in interstate commerce may raise constitutional issues concerning Congress' authority under the Commerce Clause.

Regardless of constitutional concerns, NARUC opposes the extension of FERC authority that displaces, directs or preempts State authority. At this point, no one has made the case that FERC's authority should be extended to include transmission services provided in Alaska, Hawaii, or Texas as this question would imply.

Question 11. Should States be able to discriminate against aggregators? For example, should one State be able to bar cooperatives from aggregating, while another State gives municipalities a preference by allowing forced aggregation?

Answer: NARUC has taken no position on whether Federal legislation should address the specific issue of aggregation. However, we have a long-standing position that matters involving rates and conditions of service to retail consumers should be addressed at the State level. Accordingly, NARUC does not support legislation that preempts State authority over retail services. Finally, we believe that the State legislatures and commissions have adequate authority and interest to work out fair and equitable aggregation rules and procedures without Federal involvement.

Question 12. H.R. 2944 includes aggregation language barring States from discriminating among aggregators. Have any of the 24 States that opened their retail electric markets discriminated against aggregators? If so, please identify the States and describe the discriminatory provisions.

Answer: As stated in our answer to Question 11, we believe that issues affecting retail electric service should be addressed at the State level. Issues concerning eligibility standards to aggregate retail purchases should be addressed in State legislatures and regulatory commissions.

Question 13. Mr. Brown introduced a bill (H.R. 2734) to grant municipal governments a preference in aggregating consumers, by permitting them to aggregate consumers without their express consent and preempting State laws that do not have opt out aggregation provisions. What is NARUCs position on H.R. 2734?

Answer: NARUC has taken no position on H.R. 2734.

Question 14. Some States established their own renewable portfolio standards. Is there a need to clarify State authority to impose renewable portfolio standards?

Answer: There is a need to clarify State authority to impose renewable portfolio standards. Congress should make clear that State-adopted RPS programs are permissible under Federal law, i.e. not preempted or precluded by such statutes as the Federal Power Act or PURPA, or the Commerce Clause.

Question 15. H.R. 2944 includes net metering provisions. Who should pay for new meters—the consumer, the local distribution company, or the retail electric supplier? Who should own the meters?

Answer: These issues should be left to the states, who should continue to have authority over distribution networks.

Question 16. Contractors propose amendments to provide for Federal regulation of cross-subsidies in distribution rates, require States to develop codes of conduct to prevent cross-subsidies and limit use of names and logos by utilities, and provide for enforcement of these prohibitions by State public utility commissions. What is your view of these proposals? Do States have sufficient authority to address cross-subsidy issues, or is Federal legislation necessary?

Answer: NARUC reiterates its position that retail activities should remain within the jurisdiction of State commissions. Federal legislation should clarify the authority of the States and territories to require and police the separation of utility and non-utility, and monopoly and competitive businesses. Congress should also clarify that State and territorial regulators have the ultimate and meaningful authority to ensure effective retail markets and should eliminate any barriers to the exercise of that authority by the States and territories. It is inappropriate to force small businesses and other such aggrieved parties to take their complaints to Washington for resolution. States have complaint processes to deal with local concerns. States have instituted rulemaking proceedings to impose affiliate transaction and other rules on monopoly utility companies under their jurisdiction to assure that electric customers do not subsidize non-utility ventures. Current State restructuring efforts are providing critical tools to assist State and territorial regulators in addressing market power and issues of unfair competition.

October 18, 1999

The Honorable JOE BARTON
Chairman
Subcommittee on Energy and Power
Room 2125 Rayburn Building
Washington, D.C. 20515-6115

DEAR CHAIRMAN BARTON: Thank you for your letter of October 8, 1999, and thank you again for inviting me to testify on behalf of the National Association of State Utility Consumer Advocates (NASUCA) at your Subcommittee Hearing on October 5, 1999. As I stated at that hearing, NASUCA sincerely appreciates the willingness of you and your staff to reach out in your deliberations to NASUCA members as the representatives of retail electric consumers in their respective states. NASUCA looks forward to continuing to work with you and other members of Congress as you go forward with the consideration of legislation in this vital area.

In response to the specific questions in your October 8, 1999 letter, NASUCA would respond as follows:

Question 1. Why do you believe a Federal electricity bill must include market power provisions? States have authority to address generation market power issues as they enact retail competition laws, and may order divestiture, as some have done. Also, antitrust law applies to electric utilities in competitive markets.

Response. Like electrons flowing on the grid, market power extends beyond state boundaries. Individual states do not have jurisdiction over companies or assets outside of their state borders. Antitrust laws do not adequately address market power lawfully obtained, as through the former legal and regulatory structure that existed for almost 100 years.

Question 2. Should States be able to set transmission reliability standards that supercede national and regional standards. How many States set transmission reliability standards? I understand New York is the only State that regulates transmission reliability. If New York is the only State that issues such standards, how can it be an essential State function?

Response. States do have a vital role in maintaining the reliability, safety, and adequacy of electric systems with each state's borders. All states address reliability issues in some way, even if they do not have specific regulations regarding "transmission reliability." It is NASUCA's position that states should retain authority to address all reliability matters within their state boundaries as long as their actions are not inconsistent with the actions of the new North American Electric Reliability Organization or the Federal Energy Regulatory Commission with respect to bulk power transactions in interstate commerce.

Question 3. Why tie PUHCA repeal to divestiture? In my view, PUHCA is a barrier to entry. Why should existing utilities have to sell their generation to get out from under PUHCA? How much of U.S. generating capacity is operated by subsidiaries of registered holding companies? How much of U.S. generating capacity are you proposing to divest?

Response. NASUCA does not tie PUHCA repeal to divestiture. Rather, NASUCA urges the Congress not to repeal PUHCA without first insuring that holding companies are subject to either effective competition or effective regulation where effective competition does not exist. NASUCA does not have statistics regarding generating capacity that you requested, nor does NASUCA propose a specific level of divestiture.

PUHCA still contains structural protections, vital reviews of affiliate transactions, and the federal means to order divestiture of one or more portions of a business in order to protect consumers and promote the public interest. It also prohibits utility holding companies from acquiring utility companies that provide monopoly distribution service in disparate regions.

NASUCA provides several options regarding means for protecting consumers and competition from this occurrence. Divestiture of generation is only one potential mechanism; NASUCA would expect that a showing of competitive retail generation markets for small customers in each state in which the utilities have service territories would be the primary means to address this potential problem. In addition, regulators of distribution services in each state would need to ensure that there is effective regulation to prevent utilities from gaining an unfair advantage at captive consumers' expense.

Question 4. How many of the 24 States that opened their retail markets addressed generation market power issues? Some States—Texas, California, New York, and the New England States—included generation market power provisions. Others—New Jersey and Pennsylvania—did not.

Response. NASUCA does not maintain a database that would enable a prompt response to this question. In Pennsylvania, there is, in fact, a section on "Market Power Remediation", 66 Pa.C.S. § 2811.

Question 5. The Administration bill authorizes FERC to provide backup market power remedies for retail markets at the request of States lack of authority to remedy market power. Do States lack authority to remedy market power issues?

Response. As noted in the answer to Question Number 1, states may lack authority to address some market power issues that arise beyond their borders, but that can have an impact within their borders. NASUCA would agree that states should be permitted to request FERC "backup" on market power issues that are beyond the states' own authority to address.

Response. Again, NASUCA thanks you for the opportunity to provide continued input on these issues. If you have any questions about NASUCA's position on these or any other electric restructuring issues, please contact NASUCA's Executive Director, Charles Acquard at 202-727-3908.

Sincerely yours,

IRWIN POPOWSKY, *Consumer Advocate of Pennsylvania*
Immediate Past President, NASUCA

RESPONSE OF HON. T.J. GLAUTHIER, DEPUTY SECRETARY OF ENERGY, TO QUESTIONS OF HON. JOE BARTON

Question 1. The Burr bill (H.R. 667) and the Sawyer bill (H.R. 2786) repeal section 203 of the Federal Power Act. What is your view on this proposal?

Response. We oppose the repeal of Section 203 of the FPA. As we transition from a period of monopoly utility service to competition in the wholesale and retail markets, it is imperative that we act to eliminate the impediments to competition. While utility mergers and consolidations are not *per se* inappropriate, some do have the potential to reduce competition. We need to ensure that mergers and consolidations don't actually reduce competitive pressures.

Determining whether a merger will be anti-competitive requires regulators and antitrust enforcers to make predictive judgements. These judgements are frequently difficult, and are certainly more difficult in an industry, such as electricity, where there are no fully competitive markets to use as a benchmark to determine whether a proposed merger will harm consumers.

It is important that the Federal Energy Regulatory Commission (FERC), with its significant expertise, retains its authority to ensure that proposed mergers are in the public interest. Section 203 provides FERC with the flexibility to craft appropriate policies and procedures dealing with mergers in the electric power industry over which it has jurisdiction. Section 203 also gives FERC the ability to place conditions on its merger approvals and to exercise continuing jurisdiction over the merged entities. This authority plays a significant role in preventing anticompetitive mergers, particularly during the transition period to competition.

Question 2. States have authority to address generation market power issues as they enact retail competition laws, and may order divestiture, as a number of States have done. Also, antitrust law applies to electric utilities after States cease regulating retail rates. Why is it necessary to give FERC a broad grant of discretionary authority to restructure the industry and order divestiture?

Response. The Administration bill would give FERC the authority to address wholesale market power problems. States do not have jurisdiction over sales of electricity in the wholesale market and consequently lack authority to address possible wholesale market power problems. FERC, under the Administration bill, would have backup authority to address retail market power problems. This authority can only be triggered at the request of a state. This backup authority is needed because a state may not have adequate statutory authority or jurisdiction to address market power that harms its consumers.

As we make the transition to competition, ownership patterns and transmission constraints in a particular region may result in consumers being denied access to an adequate number of generators. This situation may allow the dominant firm to raise price above competitive levels to those consumers. In those instances, it is absolutely critical that FERC be given the necessary authority to mitigate market power. The Administration bill would give FERC the authority to mitigate market power, after a public proceeding, only in those instances where it is found that a utility can exercise market power. This is not a broad authority to "restructure the industry." It is an authority to protect consumers from market power. The ultimate goal of the Administration's market power provisions is to ensure that consumers realize the benefits of competition. A failure to address adequately possible market power problems may result in replacing regulated monopolists with unregulated ones.

The antitrust laws do not outlaw the mere possession of monopoly power. In other words, the antitrust laws cannot challenge the structure of a market. For example, if, after the advent of competition, a utility possesses a 90 per cent share of a market, the antitrust laws are powerless to prevent this firm from charging monopoly prices. In order for a monopolist to violate the antitrust laws, it must engage in "bad acts," which are defined as exclusionary conduct designed to enable a firm to gain or maintain a monopoly. Charging high prices is not considered exclusionary conduct and is therefore not an antitrust violation.

Question 3. The Administration bill gives FERC extraordinary powers to order divestiture. How many Federal regulatory agencies have the power to restructure the industries they regulate, including the power to order divestiture?

Response. Section 11 of the Public Utility Holding Company Act (PUHCA) provides the SEC with the authority to require a utility holding company to simplify its corporate structure, including the authority to require divestiture. In addition, the FCC has the authority to require divestiture. The FCC has issued orders and promulgated regulations authorizing divestiture in those instances when the agency determines that divestiture is necessary to preserve competition.

It is important to keep in mind that the electric power industry is fundamentally different from other industries. All electric energy produced by all interconnected generating stations must continuously and instantaneously balance the aggregate energy being consumed by all users. Electricity cannot be economically stored. Market power remedies, such as divestiture, were probably not necessary in those industries that did not develop from government-sanctioned monopolies.

Question 4. The Administration bill would authorize FERC to order divestiture to mitigate generation market power. Aren't there less intrusive means of mitigating market power, such as reregulating retail rates charged by suppliers?

Response. It is important to note that divestiture is not the exclusive remedy that FERC would have at its disposal to address market power under the Administration proposal. FERC may find that there are other remedies that adequately mitigate market power. Re-regulating rates may not necessarily be a "less intrusive" means of mitigating market power. Rate regulation is very costly and burdensome. It requires complex rules and constant oversight and examination of a utility's sensitive records. There are constant battles over, among other things, accounting rules and proper allocation of costs. After more than a century of experience with price regulation in this industry, there is a strong consensus—which forms the foundation of the efforts to restructure the industry—that markets are superior to price regulation.

Divestiture is a common remedy used by the federal enforcement agencies to remedy likely market power caused by an anticompetitive merger. This remedy, in the merger context, preserves the competition that otherwise would have been lost. Once the assets necessary to preserve competition are sold, there is no government oversight of the firm. The market establishes the prices at which the firm's products or services are sold.

Likewise, in a restructured electric power industry, FERC would seek divestiture only when necessary to give customers an adequate number of suppliers from which to choose. Once the assets are sold that are necessary to ensure that there is competition, the market sets the prices at which energy is sold.

Question 5. You testified antitrust laws are not sufficient to address generation market power issues. Describe a market power abuse that would not violate the antitrust law.

Response. The mere possession of monopoly power does not constitute a violation of the antitrust laws. For example, an incumbent utility with a significant share of the market may be able profitably to raise price above competitive levels to consumers. This firm's choosing to exploit its market power by raising its prices above competitive levels would not constitute an antitrust violation.

Question 6. The Administration proposes a public benefits fund financed by a new tax on electric generation. This proposal is based on a theory States will slash their public benefits programs as they open retail electric markets. 24 states have opened their retail markets. How many slashed their public benefits programs? How many strengthened their programs? Why is a Federal public benefits fund needed if States maintain public benefits programs?

Response. The Administration's proposed public benefits fund does not envision any taxes. Rather, a public benefits charge (capped at 1/10 of a cent per kilowatt-hour) would be established by FERC to generate an amount sufficient to meet requests made by State and tribal governments for matching funds (subject to a $3 billion/year national cap) to support eligible public purpose programs. If no state or tribal government sought matching funds, no fees would be collected.

In addition, a wires charge of up to .17 mills per kwh would be available if the Secretary of Energy were to determine that competition has adversely impacted rural consumers. The rural safety net would be administered through the public benefits fund.

Of the states that have adopted restructuring programs, six states have decreased their funding for energy efficiency programs and eight states have increase funding for these programs.

Expenditures for public purpose programs have generally declined in recent years. For example. spending on demand-side-management programs in 1998 were approximately half the level of 1994 expenditures.

Many, but not all, states that have opened their retail markets have arranged to continue funding of public purpose programs for a limited time period. A federal public benefits fund would provide all states with an incentive to maintain such programs through 2015. Federal encouragement is appropriate given that the benefits of public purpose programs often extend beyond state boundaries.

Question 7. Legislation introduced by Mr. Pallone (H.R. 2569) includes a Federal public benefits fund different from the Administration's proposal. The Pallone bill sets different limits for State public benefits programs, imposes a distribution tax

instead of a generation tax, and is twice as large ($6 billion instead of $3 billion). What is the Administration's position on H.R. 2569?

Response. The Administration agrees with the intent of H.R. 2569—to provide a mechanism to promote expenditure on public benefits programs. Both proposals authorize the collection of a fee to help pay for State public purpose programs.

With regard to the assessment of the fee, the Administration believes that a charge on generation is more appropriate. Many distribution companies are very small. A charge of as much as 2.0 mills per kilowatt-hour, as proposed in H.R. 2569, would represent a significant increase in the costs of distribution. An additional charge of up to 1 mill (as the Administration has proposed) would not have nearly the same effect on the costs of generation.

With regard to the size of the Federal contribution to public benefits fund, the Administration believes that the Federal contribution of $3 billion and the contribution of the states at another $3 billion would be sufficient to cover what was being recovered in rates prior to the transition to more competitive markets. However, we also note that the charge envisioned in H.R. 2569 would be reduced by 50% of the amount of any wire charge imposed by a state for eligible public purpose programs. Therefore, the amount collected under H.R. 2569 is unlikely to be double the amount collected under the Administration bill.

Question 8. Some argue Federal electricity legislation should not include any consumer protection provisions, and should rely on States to address these issues. Why should consumer protection provisions be included in Federal legislation.

Response. The Administration believes that, generally, most consumer protection issues are best addressed by the states. Nevertheless, it is important to recognize that, in a competitive environment, marketers headquartered in various states will be competing for customers. State regulatory authority over unscrupulous marketers will be somewhat limited. That is why the Administration bill includes provisions designed to prevent retail suppliers from engaging and slamming and cramming practices. I understand that H.R. 2944 contains similar provisions.

Question 9. H.R. 2944 clarifies Federal and State jurisdiction, providing for FERC jurisdiction over transmission used for unbundled retail sales, and for State jurisdiction over transmission used for bundled retail sales. Is this clarification needed, and does the bill draw the jurisdictional line properly?

Response. One of the reasons Congress needs to enact electricity restructuring legislation is to ensure that FERC's open access rules apply to all significant transmission owners. FERC's current authority is limited under the Federal Power Act and, potentially, as a result of a recent 8th Circuit Court of Appeals Decision in the *Northern States Power v. FERC* case. If wholesale and retail competition are going to effectively develop, FERC must have the ability to ensure that all significant transmission facilities are subject to open access requirements. H.R. 2944 could be interpreted as limiting the applicability of FERC's open access rules to unbundled retail transmission; leaving a significant portion of transmission exempt from these open access requirements. The bill needs to be modified to eliminate this uncertainty and ensure that the open access rules apply to all transmission.

Question 10. You criticize H.R. 2944 because it does not provide for FERC regulation of transmission used to make bundled retail sales. Did the Administration bill grant FERC that authority? My understanding it did not. How can you criticize H.R. 2944 for not including something the Administration bill did not propose?

Response. The Administration's proposed legislation is silent with regard to FERC's authority over bundled retail transmission. However, our bill was transmitted to Congress prior to the 8th Circuit's decision in the *Northern States* case. This decision raises serious questions about the potential effectiveness of FERC's open access rules. Certainly, legislation must clarify that FERC has sufficient jurisdiction to ensure that utilities don't use their transmission facilities to discriminate against other marketers.

Question 11. FERC does not regulate transmission systems operated by State and municipal utilities and cooperatives, which are some of the largest systems in the country. State and municipal utilities oppose FERC regulation of transmission rates, and want to retain that authority. If State and municipal utility transmission systems continue to be unregulated could they shift power costs onto their transmission rates? Could they discriminate against competitors?

Response. If FERC were to have the authority to ensure that municipal and cooperative utilities' transmission rates are just, reasonable and not unduly discriminatory, these utilities will be on the same footing as public utilities are today, and will be unable to use their transmission systems to advantage their power systems.

Question 12. Should FERC regulate transmission that is not in interstate commerce—such as transmission in noncontiguous States and territories?

Response. The Administration believes that FERC should regulate only transmission that is in interstate commerce. Constitutional questions might arise should FERC's jurisdiction be extended to transactions not in interstate commerce.

Question 13. What is your view of the transmission provisions of the bill introduced by Mr. Sawyer (H.R. 2786)?

Response. The Administration agrees with Mr. Sawyer that transmission is a key element of promoting wholesale and retail competition. However, we are concerned about several provisions in the bill.

First, H.R. 2786 requires FERC to allow transmitting utilities to recover all costs incurred in providing transmission service. We believe that, while this is generally the appropriate policy, FERC must retain authority to review costs to ensure that they are appropriate for inclusion in rates.

Under H.R. 2786, transmission rates must be established to accomplish a number of different policy goals. We believe that these are laudable goals. However, we don't believe they should be statutorily mandated. FERC has the expertise and experience to set pricing policies appropriate to the transmission industry. On the other hand, permitting negotiated transmission rates, as H.R. 2786 does, could result in discrimination among users of the transmission system.

The Administration also agrees that FERC should encourage innovative pricing policies. However, we have concerns regarding incentive pricing to encourage participation in a regional transmission organization (RTO). The Administration believes that FERC should have the authority to require such participation, as it may not be possible to ensure a fully competitive electricity market without RTOs. For the same reason, the Administration is concerned with H.R. 2786's goal of voluntary RTO formation. In addition, there is no requirement that RTOs be independent of market participants. We agree with FERC that independence is an RTO's most important characteristic.

Question 14. H.R. 2944 includes an exemption from FERC regulation for small transmission owners. Do you believe this exemption is appropriate? Do you have any comment on the specific exemption provision in H.R. 2944?

Response. The Department of Energy supports an approach which exempts, from FERC jurisdiction, transmission facilities owned by municipal and cooperative utilities which are not essential to efficient, reliable and competitive interstate power markets.

Question 15. NARUC proposed amending the reliability title of H.R. 2944 to authorize individual States to establish reliability standards. What is your position on this proposal? Would 50 different reliability standards improve reliability? How would 50 different standards affect interstate commerce?

Response. The issue of how best to incorporate a role for the states in bulk power system reliability is complex. Certainly, a system of 50 different standards would not improve reliability, and would have an adverse impact on interstate commerce. We support a continuation of the dialogue between NARUC and NERC and other stakeholders to develop provisions that would allow for an appropriate state role.

Question 16. The reciprocity provisions of the Administration bill would grant States, municipal utilities, and cooperatives the power to regulate interstate commerce. 3,000 different entities would regulate interstate commerce (there are 2,000 municipal utilities and over 900 cooperatives). Is that wise? Since reciprocity is regulation of interstate commerce, isn't it better it be a Federal rule?

Response. While it is true that reciprocity requirements regulate interstate commerce, authorizing states and non-regulated municipal and cooperative utilities to impose reciprocity requirements is consistent with the approach taken by H.R. 2944, which leaves many matters related to interstate commerce subject to state and local regulation.

Question 17. You argue that utilities could avoid the reciprocity provisions in H.R. 2944 by filing sham open access plans with their State public utility commissions. How do you propose to address the situation where a multistate utility operates in both open and closed States? Should the utility be denied access to retail markets in the open States it has historically served?

Response. The Administration does not believe that a multistate utility should be penalized if it serves a state that requires competition and a state that has yet to require competition. However, the reciprocity provisions included in H.R. 2944, which apparently are intended to discourage utilities from acting to inhibit the introduction of retail competition, enables a utility to avoid the reciprocity restrictions simply by funding a competition plan with its state commission. There is no mechanism to ensure that the plan filed by the utility is a serious proposal and that the utility will make an effort to allow its customers access to the benefits of retail competition

Question 18. The Administration bill includes a Federal date certain with an opt out—a flexible mandate. Why do you believe the flexible mandate is needed? The real pressure on States to open their retail electric markets comes from competition with other States for economic development. The flexible mandate will result in a lot of litigation, and may not accelerate State action.

Response. The Administration believes that retail competition, if structured properly, will benefit consumers, the economy and the environment. We also believe that most, if not all, state public service commissions and non-regulated municipal and cooperative utilities would concur if they held a proceeding to review the matter. The flexible mandate approach encourages states and non-regulated utilities to implement retail competition programs but recognizes that unique local issues might require a different approach.

We disagree with your assumption that the "flexible mandate will result in a lot of litigation . . ." The opportunities for challenging the decision of a state public service commission or a non-regulated utility to opt-out are limited.

Question 19. A number of States have established their own renewable portfolio standards. Is there a need to clarify State authority to impose renewable portfolio standards, or is there no doubt States have such authority?

Response. We are unaware of any challenges to the authority of states to adopt renewable portfolio standards. In addition, we believe states would have the ability to impose a renewable portfolio standard and require a higher amount of renewable generation if a Federal renewable portfolio standard is enacted.

The Administration believes that the limited programs that have been adopted in a small number of states cannot provide the significant national benefits that would result from the adoption of a national renewable portfolio standard that requires all retail sellers to cover 7.5% of their sales with generation from eligible renewable resources by 2010.

Question 20. Does the Administration support the bill introduced by Mr. Waxman to amend the Clean Air Act to require older coal power plants in the Midwest and Southeast to meet new source performance standards (H.R. 2900)?

Response. The Administration has not yet taken a position on H.R. 2900.

Question 21. The Administration bill includes aggregation language similar to the aggregation provisions in H.R. 2944. Have any of the 24 States that opened their retail electric markets discriminated against aggregators? If so, please identify the States and describe the discriminatory provisions.

Response. Maryland, which adopted retail competition legislation, prevents municipalities from acting as aggregators. In addition, it is not entirely clear that all states permit the rural electric cooperatives operating within their borders to aggregate on behalf of their distribution customers.

Question 22. Mr. Brown introduced a bill (H.R. 2734) to grant municipal governments a preference in aggregating consumers, since it permits them to aggregate consumers without their consent. What is the Administration's position on that bill? Should municipalities have an advantage in aggregating over churches, social and charitable organizations, and others?

Response. The Administration believes that aggregation is an important tool to ensure that residential and small commercial electricity consumers reap the full benefits of retail competition programs. It is the Administration's position that municipalities and all other entities should be able to aggregate groups of consumers. At the same time, we don't believe that any aggregator should be able to force a consumer to be served by that entity. We don't read the Brown bill as forcing any consumer to be served by a municipal aggregator.

Question 23. The Administration bill includes interconnection provisions similar to H.R. 2944. Will these provisions lower barriers to entry for new power plants?

Response. Interconnection standards in the Administration bill apply specifically to small-scale distributed generation facilities and combined heat and power facilities. These provisions lower a potentially important barrier to entry for those new power plants that fail within these categories. Unwarranted impediments to interconnection provide a means for incumbent utilities to prevent entry and exert market power. Moreover, interconnection standards vary widely from utility to utility thereby discouraging widespread use of distributed generation. For these reasons, the Administration proposes a provision to establish and implement national uniform, and non-discriminatory technical interconnection standards for the hookup of distributed power generation systems to distribution utilities.

Question 24. The Administration bill promotes interconnection of "small scale electric power generation facilities" of undefined size, and H.R. 2944 promotes interconnection of distributed generation facilities of 50 megawatts or less. Should distributed generation facilities be of unlimited size? Are there reliability implications if these facilities are too large?

Response. We believe that distributed power is likely to play a significant role in meeting customer needs in restructured electricity markets. The Administration bill does not set a specific size threshold for distributed generation facilities because we believe that the definition of a "small-scale electric power generation facility" should be determined based on technical considerations. A working group under the Institute of Electrical and Electronics Engineers is already developing a voluntary industry standard for interconnecting distributed power with electric distribution and subtransmission systems, and plans to have a complete draft ready by March 1999 to start the consensus process. We understand that the current draft envisions voluntary standards applicable to facilities up to 50 megawatts in size, but this is clearly subject to further technical deliberation.

Question 25. The Administration bill includes net metering provisions similar to H.R. 2944. Who should pay for new meters—the consumer, the local distribution company, or the retail electric supplier? Who should own the meters?

Response. The Administration believes that questions concerning the ownership of and payment for distribution meters should be addressed at the state level. In this regard, meters used for net metering are no different from other distribution meters. However, given the national interest in increased use of renewable energy technologies, the Administration's restructuring proposal would insure that net metering service is made available to consumers in all parts of the country who wish to install small-scale renewable energy technologies.

THE ELECTRICITY COMPETITION AND RELIABILITY ACT

WEDNESDAY, OCTOBER 6, 1999

HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON ENERGY AND POWER,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m. in room 2123, Rayburn House Office Building, Hon. Joe Barton (chairman) presiding.

Members present: Representatives Barton, Stearns, Largent, Burr, Whitfield, Shimkus, Wilson, Pickering, Fossella, Bryant, Ehrlich, Hall, McCarthy, Sawyer, Markey, and Wynn.

Staff present: Joe Kelliher, majority counsel; Cathy Van Way, majority counsel; Miriam Erickson, majority counsel; Ramsen Betfarhad, economic advisor; Elizabeth Brennan, legislative clerk; Sue Sheridan, minority counsel; and Rick Kessler, minority professional staff member.

Mr. BARTON. The Subcommittee on Energy and Power of the Commerce Committee will come to order.

Today is a continuation of a hearing that we began yesterday, a legislative hearing on the pending piece of legislation, H.R. 2944.

Today we are going to begin hearing from groups out in the country that have an interest in this. I think we have a total of 17 witnesses in two panels, and I believe that we have accepted every witness request from every member of the subcommittee on both sides of the aisle.

I will make this announcement periodically during the day, as more members show up, but it is unlikely we will go to markup next week because the full committee is going to try to mark up a Superfund bill that Congressman Oxley is working on in his subcommittee, but it is the Chair's intention to spend the rest of this week and next week getting input from members and interest groups on specific legislative language and specific changes to H.R. 2944, and then the following week—not next week, but the week after next—to schedule a markup. And I will do that in conjunction with Chairman Bliley and Congressman Hall and Congressman Dingell in terms of actually scheduling a date certain for a markup. But it is my intention to do that not next week but the week after next.

With that, we want to begin to hearing testimony. We are going to start with Mr. William Helton, which is somewhat different. Normally, we go from the Chair's left to right, but we are going to

go from the Chair's right to left because that is the way we have it in the witness list.

So, Mr. William Helton is with New Century Energies, and he represents the Alliance for Competitive Electricity.

Your statement is in the record in its entirety. We ask that you summarize it in, let's say, 6 minutes. How about that?

Welcome to the committee.

STATEMENTS OF WILLIAM HELTON, NEW CENTURY ENERGIES, REPRESENTING ALLIANCE FOR COMPETITIVE ELECTRICITY; DAVID R. NEVIUS, VICE PRESIDENT, NORTH AMERICAN ELECTRIC RELIABILITY COUNCIL; ALAN H. RICHARDSON, EXECUTIVE DIRECTOR, AMERICAN PUBLIC POWER ASSOCIATION; DAVID K. OWENS, EXECUTIVE VICE PRESIDENT, EDISON ELECTRIC INSTITUTE; LYNNE H. CHURCH, EXECUTIVE DIRECTOR, ELECTRIC POWER SUPPLY ASSOCIATION; WILLIAM R. MAYBEN, PRESIDENT, NEBRASKA PUBLIC POWER DISTRICT, REPRESENTING LARGE PUBLIC POWER COUNCIL; GLENN ENGLISH, CHIEF EXECUTIVE OFFICER, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION; DAVID G. HAWKINS, DIRECTOR OF AIR AND ENERGY PROGRAMS, NATURAL RESOURCES DEFENSE COUNCIL; AND RAJESHWAR RAO, PRESIDENT, INDIANA MUNICIPAL POWER AGENCY, REPRESENTING TRANSMISSION ACCESS POLICY STUDY GROUP

Mr. HELTON. Mr. Chairman and members of the subcommittee, I am Bill Helton, chairman and chief executive officer of New Century Energies. New Century Energies serves over 1.5 million electric and 1 million gas customers in portions of six western States, including Colorado, New Mexico, Texas, Wyoming, Kansas, and Oklahoma. Three of the States we operate in—New Mexico, Oklahoma, and Texas—already have adopted customer choice legislation.

We support providing customers with a choice of their electric supplier and are working in our other States to achieve that very objective.

I also am testifying today on behalf of the Alliance for Competitive Electricity, an organization of 11 investor-owned utilities formed nearly 4 years ago for the purpose of promoting Federal restructuring legislation to foster a more-competitive electric industry.

Ten of our 11 members operate in States that already have adopted retail choice plans. Now, these States include: California, New Mexico, Texas, Oklahoma, Michigan, Pennsylvania, New Jersey, Massachusetts, Rhode Island, New Hampshire, Maine, Virginia, and Arkansas.

The Alliance has endeavored to be an interested, credible broker on many difficult restructuring issues.

Mr. Chairman, as you know better than anyone, addressing the Federal issues associated with restructuring the $220 billion electric industry has proven to be complex, controversial, and mostly thankless task.

I personally want to take this time to thank the committee for its time and energy, attention, and perseverance, and, in many

cases, good humor that you have brought to bear on this issue, and for doing the hard work that needs to be done to get to the finish line.

I also want to thank you and your staff for listening to our ideas and our suggestions and our comments on the August 4 staff discussion draft.

Mr. Chairman, H.R. 2944 is not a perfect bill, from our perspective, but it is a good one that fairly addresses most Federal electric industry restructuring issues in a reasoned and balanced way.

At your very first hearing on electric industry restructuring issues in this Congress, you asked a distinguished panel of witnesses whether, if certain key Federal restructuring issues could be addressed, but not all of them, would it make sense to pass a good, albeit not perfect, bill.

Three of your witnesses all indicated that it was important not to let the perfect be the enemy of the good, and there was an urgency to dealing with a number of restructuring issues, including reliability. That was good advice then and that is good advice today.

As we work toward implementing customer choice in the three States that we serve that have adopted this as their policy, it is becoming increasingly clear that, despite the primary role the States must play, the States do not have the jurisdiction or the authority to do all that is necessary.

For example, the States cannot deal with the Federal barriers that now stand in the way of a more competitive industry, including PUHCA and PURPA.

The States cannot clarify State/Federal jurisdictional ambiguity that threatens FERC order number 988 and State restructuring plans.

The States, additionally, cannot extent FERC's transmission regulation, including FERC's open access policies, to non-FERC jurisdictional transmission owners, including TVA and the PMAs.

The States cannot reform the PMAs or the TVA to allow the consumers they serve to obtain the benefits of a more-competitive electricity market.

The States cannot insure the reliability of the interstate transmission grid.

And, last, the States cannot establish a new regulatory regime governing the transmission system that ensures open, non-discriminatory access.

The States cannot do these many things that need to be done to bring all consumers the benefits of a more-competitive electric industry. So, regardless of your position or your State's position on retail customer choice, much must be done in Congress in order to help smooth the restructuring path.

We believe that your bill satisfactorily addresses most of these core Federal issues. In particular, we are pleased the way the bill addresses uniform regulation and open access for all transmission owners. We are pleased the way it addresses the clarification of State/Federal regulatory jurisdiction. We are pleased with the bill's assist in insuring reliability of the bulk power system. We are also pleased in the way it addresses that States should be given explicit authority to impose charges on jurisdictional activities. Also, the

bill does a good job in addressing FERC's regulation that it should be extended to PMA's TVA energy sales rates.

The bill adequately covers the repeal of PUHCA and PURPA.

Mr. Chairman, these issues that I have mentioned must be at the core of any comprehensive Federal electric industry restructuring legislation, and all are addressed satisfactorily in H.R. 2944.

We remain concerned, however, over the private use and the co-op tax relief provision contained in H.R. 2944 and believe that BPA, TVA, regional transmission organization, reciprocity, merger review, aggregation, and interconnection provisions can be improved without fundamentally changing your intent.

We will be developing perfecting legislative language to accomplish those improvements.

H.R. 2944 does a great deal to mitigate market power. The bill requires utilities to turn over operational control of their transmission systems to an independent RTO that allows customers to band together——

Mr. BARTON. Mr. Helton, can I ask you to summarize. You have gone past your 6 minutes.

Mr. HELTON. Yes, sir.

Mr. BARTON. We want to move this panel on.

Mr. HELTON. In conclusion, Mr. Chairman——

Mr. BARTON. Very good. Fast learner.

Mr. HELTON. I want to thank you and the other members of the subcommittee for the good work that you have done. H.R. 2944 reflects your tireless efforts to seek compromising consensus. From any perspective, it is basically a good bill worthy of support.

[The prepared statement of William Helton follows:]

PREPARED STATEMENT OF BILL HELTON, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, NEW CENTURY ENERGIES, ON BEHALF OF THE ALLIANCE FOR COMPETITIVE ELECTRICITY

I. INTRODUCTION

Mr. Chairman and Members of the Subcommittee, I am Bill Helton, Chairman of the Board and Chief Executive Officer of New Century Energies. New Century Energies serves over 1.5 million electric and natural gas customers in portions of six Western states, including Colorado, New Mexico, Texas, Wyoming, Kansas and Oklahoma. Three of the states we operate in, New Mexico, Oklahoma and Texas, already have adopted customer choice legislation. We support providing customers with a choice of their electric supplier and are working in our other states to achieve that objective.

I also am testifying today on behalf of the Alliance for Competitive Electricity, an organization of 11 investor-owned utilities formed nearly 4 years ago for the purpose of promoting federal restructuring legislation to foster a more competitive electric industry. Ten of our 11 Members operate in states that already have adopted retail choice plans. These states include California, New Mexico, Texas, Oklahoma, Michigan, Pennsylvania, New Jersey, Massachusetts, Rhode Island, new Hampshire, Maine, Virginia, and Arkansas. The Alliance has endeavored to be an interested, credible, broker on many difficult restructuring issues.

Mr. Chairman, as you know better than anyone, addressing the federal issues associated with restructuring the $220 billion a year electric industry has proven to be a complex, controversial, and mostly thankless, task. I personally want to thank you for the time, energy, attention, perseverance, and good humor that you have brought to bear on this issue and for doing the hard work that needs to be done. I also want to thank you and your staff for listening to our ideas, suggestions, and comments on the August 4 staff discussion draft.

Mr. Chairman, H.R. 2944 is not a perfect bill from our perspective. But it is a good one that fairly addresses most federal electric industry restructuring issues in a reasoned and balanced way.

At your very first hearing on electric industry restructuring issues in this Congress, you asked a distinguished panel of witnesses whether if certain key federal restructuring issues could be addressed, but not all of them, it would make sense to pass a good, albeit not perfect, bill. Three of your witnesses, former Deputy Secretary of Energy and former FERC Chair Elizabeth Moler, former FERC Commissioner Michael Naeve, and former Deputy Secretary of Energy Linda Stuntz all indicated that it was important not to let the perfect be the enemy of the good and that there was an urgency to dealing with a number of restructuring issues, including reliability. That was good advice then, and it remains good advice today.

II. THE ROLE OF CONGRESS

As we work toward implementing customer choice in the three states we serve that have adopted this as their policy, it is becoming increasingly clear that, despite the primary role the states must play in restructuring the electric industry, the states do not have the jurisdiction or the authority to do all that is necessary. For example, the states cannot deal with the federal barriers that now stand in the way of a more competitive industry, including PUHCA and PURPA; the states cannot clarify state/federal jurisdictional ambiguity that threatens FERC Order No. 888 and state restructuring plans; the states cannot extend FERC's transmission regulation, including FERC's open access policies, to non-FERC jurisdictional transmission owners, including TVA and the PMAs; the states cannot reform the PMAs or the TVA to allow the consumers they serve to obtain the benefits of more competitive electricity markets; the states cannot ensure the reliability of the interstate transmission grid; and the states cannot establish a new regulatory regime governing the transmission system that ensures open, non-discriminatory access, while providing the incentives necessary to upgrade and expand that system. The states cannot do these many things that need to be done to bring all consumers the benefits of a more competitive electric industry. So, regardless of your position, or your state's position, on retail customer choice, much must be done in Congress in order to help smooth the restructuring path.

We believe that your bill satisfactorily addresses most of these core federal issues. In particular, we are pleased with the provisions addressing the following:

- **Uniform Regulation and Open Access for All Transmission Owners**—While investor owned utilities are subject to FERC regulation of the rates, terms and conditions applicable to the provision of transmission service, municipal and state utilities, co-ops, TVA, and the PMAs are not. As a consequence, only about 70% of all transmission is subject to FERC regulation, including wholesale open access requirements. This creates an untenable situation. FERC jurisdiction should be extended to all transmission owners in the lower 48 states. With the possible exceptions of TVA and BPA, which continue to be treated as "special" in certain respects, H.R. 2944 would satisfactorily accomplish this.
- **Clarification of State/Federal Regulatory Jurisdiction**—As we move to a new regulatory system in which the various components of electric service are "unbundled," it is clear that the Federal Power Act, which was written at a time when retail sales were "bundled," needs to be updated. A clear new "bright line" between state and federal regulatory jurisdiction needs to be drawn. States should be given exclusive regulatory authority over bundled retail sales, over the retail sale component and the local distribution service component of an unbundled retail sale, and over the "service" of delivering retail electricity. FERC should be given exclusive jurisdiction over the transmission component of an unbundled retail sale and should retain its exclusive jurisdiction over wholesale sales and transmission. This "bright line" was spelled out in FERC Order No. 888, and it represents a reasonable and fair division of regulatory authority. H.R. 2944 adopts this position.
- **Help Ensure Reliability of Bulk Power System**—Our existing voluntary reliability organizations have served us well. However, with the advent of EPAct, FERC Order No. 888 and retail competition, the transmission system is being stressed as never before. In addition, there are hundreds of new entrants in the electric market that make it more difficult to manage the system using voluntary reliability standards. Virtually all industry participants believe strongly that new, enforceable, reliability standards need to be adopted to help ensure that our transmission system continues to operate safely and reliably. Consensus reliability legislation has been developed by the NERC, and is, in most material respects, included in H.R. 2944.
- **States Should be Given Explicit Authority to Impose Charges on Jurisdictional Activities**—States, in carrying out their exclusive jurisdiction over retail sales and local distribution, should be given explicit authority to require the

payment of charges deemed necessary to recover retail transition and stranded costs; to ensure adequate supply and reliability; to assist low-income customers; to encourage environmental, renewable energy, energy efficiency or conservation programs; to provide for assistance to electric utility workers adversely affected by restructuring; and to encourage research and development. H.R. 2944 would do this.

- **FERC Regulation Should be Extended to PMA and TVA Energy Sales Rates**—The PMAs and TVA essentially regulate their own rates. In the new, competitive wholesale and retail marketplace, this is an anachronism that could lead to unfair competition. FERC jurisdiction should be extended to PMA and TVA sales. Both wholesale and retail sales of capacity and energy should be covered. In addition, the FERC should use Federal Power Act rate making and accounting standards to carry out this new authority to ensure that both IOUs and federal power agencies are regulated in a similar manner. H.R. 2944 takes significant steps toward accomplishing this.
- **The Public Utility Holding Company Act of 1935 ("PUHCA") Should be Repealed**—PUHCA is serving as an impediment to competition. It should be repealed. H.R 2944 adopts consensus language that would repeal PUHCA one year after the date of enactment.
- **The Purchase Mandate in the Public Utility Regulatory Policies Act of 1978 ("PURPA") Should be Repealed and Costs Recovered**—PURPA has long outlived its usefulness. It is costing consumers billions of dollars a year in excess power costs and is inconsistent with competitive generation markets. The purchase mandate in section 210 of PURPA should be prospectively repealed; existing contracts protected; and full recovery of PURPA costs assured. H.R. 2944 includes the Stearns consensus legislation that would accomplish this.
- **Transmission Policies Should be Updated**—EPAct, FERC Order No. 888, and FERC's Regional Transmission Organization ("RTO") Notice of Proposed Rulemaking have created unparalleled regulatory uncertainty with respect to the interstate transmission of electricity. Congress should establish clear standards with respect to RTOs, while giving industry the flexibility to develop appropriate independent organizations to manage the operation of transmission facilities. H.R. 2944 establishes a framework that would accomplish these important objectives. We believe, however, that some changes to the RTO language may be appropriate and we hope to work with the Subcommittee on these as the process goes forward.

Mr. Chairman, these issues that I have mentioned must be at the core of any comprehensive federal electric industry restructuring legislation, and all are addressed satisfactorily in H.R. 2944. We remain concerned, however, over the private use and coop tax relief provisions contained in H.R. 2944 and believe that the BPA, TVA, RTO, reciprocity, merger review, aggregation and interconnection provisions can be improved without fundamentally changing your intent. We will be developing perfecting legislative language to accomplish these improvements. Some of our members also are concerned about the merger provisions of H.R. 2944. These provisions would expand FERC authority to review the retail aspects of mergers and asset dispositions, ostensibly for purposes of addressing market power concerns. Such power is already resident, both in authority and practice, in the Department of Justice and the Federal Trade Commission under existing antitrust laws. The addition of duplicate review of areas that are currently beyond FERC jurisdiction raises concerns of opportunities for market meddling, a problem that will stifle full competitive development.

I am sure others have concerns that the bill does not go far enough in expanding FERC authority over transmission (thereby displacing the states) or that not enough is being done to address "market power," a flexible term that is being used to justify a whole host of utility market restrictions.

H.R. 2944, in fact, does a great deal to mitigate market power. Your bill:

- requires utilities to turn over operational control of their transmission systems to independent RTOs, something Congress has never required of any other network industry;
- allows customers to band together to aggregate load, thereby gaining negotiating leverage; and
- establishes uniform federal interconnection standards, thereby increasing competition.

At the same time H.R. 2944 increases regulatory authority in these areas, it carefully preserves the array of authorities that already exist. For example, your bill does not:

- displace or preempt state authority to regulate retail rates;

- eliminate or curtail FERC authority to regulate wholesale rates;
- diminish in any way Department of Justice or Federal Trade Commission authority under existing antitrust laws or limit private rights of action under these laws.

What advocates of "market power" amendments are asking you to do is to disable particular competitors, not *enable* competition. I urge this Subcommittee not to get into the business of favoring one competitor over another.

III. CONCLUSION

Mr. Chairman, I again want to thank you and the other Members of the Subcommittee for the good work that you have done. H.R. 2944 reflects your tireless efforts to seek compromise and consensus. From any perspective, it is a good bill worthy of support.

Mr. BARTON. Thank you, Mr. Helton.

Be advised that all your testimony is in the record. Many members have reviewed that, so we ask to try to hold to the 6 minutes. I thank you for your testimony.

The next is Mr. David Nevius, vice president of the North American Electric Reliability Council from Princeton, New Jersey.

Welcome. You have 6 minutes. Your full testimony is in the record.

STATEMENT OF DAVID R. NEVIUS

Mr. NEVIUS. Thank you very much.

NERC applauds the subcommittee chairman for including the NERC consensus reliability language in title II of H.R. 2944. We also commend the other members of the subcommittee who have advanced other bills containing the NERC consensus language.

I have submitted the prepared remarks for the record, in which we support prompt enactment of reliability legislation contained in title II of H.R. 2944, with just a few modifications, and we have alerted your staff of where those issues are.

Being part of this large panel, with another panel to follow on the second day of your hearings, I am going to be very brief.

My single but very, very important message to you all is: we need reliability legislation now.

Without the ability to enforce compliance with mandatory reliability rules fairly applied to all participants, we may not be able much longer to keep the interstate electronic grids operating reliably.

Thank you. I look forward to your questions.

[The prepared statement of David R. Nevius follows:]

PREPARED STATEMENT OF DAVID R. NEVIUS, VICE PRESIDENT, NORTH AMERICAN ELECTRIC RELIABILITY COUNCIL

The North American Electric Reliability Council (NERC) firmly believes that there is an urgent need for Federal legislation to establish an independent, industry self-regulatory electric reliability organization (ERO) to ensure the continued reliability of the interstate (and international) high-voltage transmission grids. These grids are critical to public health, safety, welfare, and national security throughout North America.

Title II of H.R. 2944, "Electric Reliability," would establish such an ERO that would develop and enforce mandatory reliability rules, with FERC providing oversight in the U.S. to make sure the ERO and its affiliated regional reliability entities operate effectively and fairly. Similar oversight would be provided by government entities in Canada and Mexico. NERC applauds the Subcommittee chairman for including the NERC consensus language in Title II of H.R. 2944. NERC also commends other members of the Subcommittee who have advanced bills containing the NERC consensus language.

Three issues need further consideration in H.R. 2944:

FERC Authority to Establish Interim Standards and Procedures—H.R. 2944 includes two additions to the NERC consensus language that are problematic. These additions direct the Commission to: (1) establish interim reliability standards if it suspends any previously approved standards, pending development of new standards; and (2) establish interim procedures or governance or funding provisions if it suspends any previously approved provisions, pending development of new provisions. NERC believes that this language needs further work. The underlying philosophy of a self-regulatory organization is that it be afforded every opportunity to make any necessary modifications to its own standards and procedures before a regulatory body steps in to establish standards and procedures on its own. This is doubly important in the case of the ERO because it is intended to have shared oversight by governmental bodies in Canada, Mexico, and the United States. Any such interim standards established by the Commission could have negative reliability or trade impacts on Canada or Mexico, on which they would have no opportunity for input. There may be helpful guidance for resolving this issue in the securities industry context. For example, Section 19 (c) of the Securities and Exchange Act provides the SEC with the power to modify a self-regulatory organization's rules, but does so in a manner that (1) gives the self-regulatory organization an opportunity to modify its own rules and (2) specifies detailed procedures calling for notice and public participation that the SEC must follow. The nature of these procedures encourages the self-regulatory organizations to modify their own standards and procedures, rather than have something imposed by the SEC. NERC is working with other supporters of its consensus language and will offer proposed alternative language to the Subcommittee staff for consideration.

Role of the States—Recently, proposals have been made to add language to the NERC consensus language defining the role of States in ensuring reliable electric service to retail consumers. This is an important and complex issue that must be resolved. Representatives of industry organizations and the States are working to resolve this issue literally as we speak, and NERC strongly supports these efforts.

Avoiding Statutory Ambiguities—Provisions of the existing Federal Power Act contain definitions that create an ambiguity as to the scope of the reliability title. For example, Section 201(f) states that no provision of Part II of the Federal Power Act applies to the United States, a State, or any political subdivision thereof, or to any agency of any of those unless the provision expressly so states. The reliability title is clearly intended to apply to all entities, regardless of ownership. To avoid such ambiguities, NERC suggests adding a phrase at the beginning of what would be new Section 217(b)(1) [H.R. 2944, page 34, line 19] to read: (b) Commission Authority—"Notwithstanding any other provision of the Federal Power Act, . . ." Such an addition would allow the provisions of Title II of H.R. 2944 to stand alone and independent of any existing or future provisions of the Federal Power Act.

NERC supports prompt enactment of any legislation containing Title II—Electric Reliability of H.R. 2944. The existing scheme of voluntary compliance with industry reliability rules for the high-voltage grid system is simply no longer adequate. The rules must be made mandatory and enforceable, and fairly applied to all participants in the electricity market. Even after enactment of this reliability legislation, it will take some time to complete the necessary rule making and gain the required approvals before the ERO can actually begin operation. The longer it takes to establish this new system, the greater becomes the risk and magnitude of grid failures.

The users and operators of the system, who used to cooperate voluntarily under the regulated model, are now competitors without the same incentives to cooperate with each other or comply with voluntary reliability rules.

NERC is seeing a marked increase in the number and seriousness of violations of its reliability rules, yet there is no recourse under the current voluntary model to correct this behavior.

Market participants are increasingly asking FERC to make decisions on reliability issues for which FERC does not have either the technical expertise or direct, clear statutory authority. The indirect, limited authority FERC does have regarding reliability applies to only two-thirds of the Nation's transmission facilities-co-ops, municipalities, the federal power marketing administrations, the Tennessee Valley Authority, and ERCOT utilities are outside its jurisdiction—and FERC has no authority in Canada or Mexico.

The bottom line is that not a single bulk-power system reliability standard can be enforced effectively today, by NERC or the Commission.

NERC urges the members of the Energy and Power Subcommittee and the full Commerce Committee to push ahead aggressively with this much needed reliability legislation. The continued reliability of North America's high-voltage electricity grids and all the customers who depend on them are at stake.

In Closing . . .

- A new electric reliability oversight system is needed now.
- An industry self-regulatory system is superior to a government system for setting and enforcing compliance with grid reliability rules.
- Title II—Electric Reliability of H.R. 2944, with just a few modifications, will allow for the timely creation and oversight of a viable self-regulatory reliability organization.
- The longer it takes to establish this new system, the greater becomes the risk and magnitude of grid failures.
- The reliability of North America's interconnected transmission grids need not be compromised by changes taking place in the industry, provided reliability legislation is enacted now.

Mr. BARTON. You really learn rapidly. The chairman is going to be so pleased with my stewardship here. Thank you, Mr. Nevius.

Next we have Mr. Alan Richardson, executive director of the American Public Power Association from Washington, DC.

STATEMENT OF ALAN H. RICHARDSON

Mr. RICHARDSON. Thank you, Mr. Chairman. I was going to ask for the balance of Mr. Nevius' time until I heard the applause.

Mr. BARTON. I think there would be an objection.

Mr. RICHARDSON. It is a pleasure to be here again testifying before you.

APPA believes that there is a need for and supports the enactment of comprehensive Federal restructuring legislation that facilitates State electric utility restructuring initiatives by clarifying Federal areas of jurisdiction that remove interstate commerce and Federal tax code barriers to competition.

We believe Congress should pass legislation because these issues are solely within the jurisdiction of the Federal Government, and Federal legislation is essential to put in place the industry structure that will make wholesale competition and retail deregulation plans work effectively.

The key to effective and sustained competition is putting in place the proper structure, and the key to the proper structure is getting transmission right.

I think the requirements are quite simple. We need large regional transmission grids that mirror regional power markets. The grids must be operated, maintained, planned, and constructed on a competitively neutral basis. That is, they must be completely independent, and they must encompass all facilities that comprise the interconnected grid.

There are several provisions of the bill that would make it difficult to achieve these objectives. For example, FERC's jurisdiction over vast amounts of transmission facilities may well diminish if these facilities with State acquiescence are redefined or refunctionalized as State jurisdictional distribution facilities.

More troubling to us, FERC is not given the authority to establish regional boundaries. Incumbent utility proposals for RTOs are more likely than not to have boundaries dictated by the competitive interests of the generation owners and not by the regional markets. We think the only way to get there is to permit FERC to establish these borders to give all stakeholders reasonable time in consensus negotiations to create RTOs that match those borders, ensure a process that protects the rights and interests of participants, and provides backstop authority for the Commission, as appropriately

conditioned, as indicated in my testimony, to get the job done if the negotiations fail to produce the appropriate result.

Another problem that we see with H.R. 2944 is that it undermines the essential requirement of independence and competitive neutrality of RTOs. Passive ownership of up to 10 percent voting interest per participant will not guarantee independence—in fact, just the opposite.

Incentive rates for the creation of RTOs and extending incentives to participants in existing RTOs is, in our view, inappropriate; however, incentives are appropriate to remove constraints and reward superior performance.

H.R. 2944 is deficient in dealing with utility mergers and addressing generation horizontal market power. While reasonable steps should be utilized to prevent protracted proceedings, in the end protecting the public interest is far more important than expedited consideration of proposals to advance private corporation interests.

Protecting the public interest includes preserving the opportunity for full evidentiary hearings to analyze merger proposals where that is necessary.

We do support the expansion of FERC's authority over holding company mergers and the required consideration of how proposals brought to the Commission could affect competition in transmission and generation markets. However, the benefits of these changes may well be more than offset by the changes in the merger review process and the unreasonably short deadline set for intervener participation in Commission proceedings.

Horizontal market power should also be addressed. Generation power may not be a long-term problem, but it is a significant problem in the transition phase because we start with such high degrees of concentration in particular markets, aggravated by significant transmission constraints.

FERC should be able to deal quickly and effectively with the exercise of generation market power. It should be given a toolbox of potential remedies to deal with these issues that remain at its disposal until it reports to Congress that the transmission system is regional in scope, competitively neutral, and adequate to provide competition in generation markets throughout the country.

Finally, the expansion of full-blown jurisdiction over transmission facilities of publicly owned utilities contained in this legislation appears to us to be a solution in search of a problem.

Jurisdiction beyond that absolutely necessary to ensure comparability is unnecessary.

Those are our concerns. Let me identify a few issues that we support.

We do support the reliability title strongly. There are still some glitches to be worked out, but we believe it is essential that it be included and that it be passed.

We support the aggregation provisions and are pleased that units of State and local government are specifically authorized to perform this function for their own citizens.

We support the renewable resource provisions, although with some reservations, as noted in my statement.

And we support, most of all, H.R. 2944's proposed resolution of public power's private use problem. Private use is a critical problem for public power with taxing and financing transmission and generation facilities. If it is not addressed, many of these systems will be forced to opt out of competition, because if they do not opt out they put their consumers, communities, and bondholders in jeopardy. However, over time, opting out is simply politically impossible; therefore, we are in a bind.

H.R. 721, the Bond Fairness and Protection Act, is a fair and equitable resolution to the problem. It has been incorporated, for the most part, in H.R. 2944. We believe this is a very positive step forward in resolving this real problem. We hope the original language of that bill, H.R. 721, can be restored, and we hope no further changes in that legislation are permitted as this or a successor bill moves through the subcommittee.

Mr. Chairman, thank you for the opportunity to testify. I appreciate it. And I look forward to answering your questions.

[The prepared statement of Alan H. Richardson follows:]

PREPARED STATEMENT OF ALAN H. RICHARDSON, EXECUTIVE DIRECTOR, AMERICAN PUBLIC POWER ASSOCIATION

Mr. Chairman, members of the subcommittee, my name is Alan Richardson. I am the executive director of the American Public Power Association. APPA is the national service organization representing the interests of the nation's nearly 2,000 publicly owned, locally controlled, electric utilities, providing electric service to nearly 40 million Americans.

You have asked us to address four questions. First, whether APPA believes there is a need for Federal electricity legislation. Second, if so, why Congress should pass such legislation. Third, what specific elements should be included in such legislation. And fourth, to discuss the provisions of H.R. 2944, the Electricity Competition and Reliability Act .

NEED FOR FEDERAL LEGISLATION

APPA has consistently advocated the enactment of comprehensive Federal electricity restructuring legislation that facilitates state electric utility restructuring initiatives by clarifying state and Federal areas of jurisdiction, and that removes interstate commerce and federal tax code barriers to competition that are solely within the jurisdiction of the U.S. Congress.

There is only one reason for Congress to enact comprehensive electric utility restructuring legislation—to promote competition for the benefit of all consumers. The overriding objective must be to restructure the industry in a way that has a high probability of benefiting all classes of customers with no degradation of reliability of service.

The abuse of existing market power, aggravated by the accumulation of ever increasing control over transmission and generation in the hands of an ever decreasing number of players is the biggest single obstacle to the realization of this objective and the creation of robust competition in the electric utility industry.

Evidence that both of these factors exist—abuse of existing market power, and the ever increasing control over essential facilities in the hands of decreasing number of players—abounds. Attached to my statement is a list, on a year-by-year basis, of investor-owned utility mergers and acquisitions, plant acquisitions, transactions involving Foreign utilities, and holding companies established. The sheer magnitude of the change in the structure of the industry in the past two years alone is overwhelming. Even more significant is the accelerating pace of this change. In the first nine months of 1999 alone, investor owned utilities have announced or consummated 30 mergers or major acquisitions, compared to 12 the year before.

There is nothing coincidental about this trend. It can be traced directly to the open transmission access provisions of the Energy Policy Act of 1992, the aggressive implementation of that Act by the Federal Energy Regulatory Commission two years later, combined with state legislative restructuring initiatives that began less than five years ago. As FERC tried to break open the transmission grid to promote wholesale competition, and states have tried to create an environment conducive to

retail competition, the vertically integrated investor owned utility monopolies, while paying lip service to competition, have been taking dramatic steps to consolidate their control of both the transmission grid and the generation market.

As noted by Albert A. Foer, president of the American Antitrust Institute, Inc., in his article "Institutional Contexts of Market Power in the Electricity Industry" published in the May, 1999 issue of *The Electricity Journal*, "the ongoing wave of utility mergers, apparently in strategic preparation for restructuring, has the potential to nullify the objective of opening up markets. Many mergers involving adjacent geographic markets appear to be aimed at expanding the incumbency advantages prior to restructuring."

The evidence of the abuse of market power, and the urgent need to address it through Federal restructuring legislation, is abundantly clear from the hearing record of this subcommittee. The vast majority of witnesses with very diverse constituencies and interests that have appeared at subcommittee hearings over the past three years have pleaded for legislation to address this problem. Virtually alone on the other side of this debate of whether market power problems exist are the investor owned utilities. They deny the existence of significant market power problems, counsel against any legislation to deal with such problems, and seek further protection.

WHY SHOULD CONGRESS ENACT LEGISLATION?

The market power problems that exist, as well as those that we can now predict with a great degree of certainty, can only be addressed by Congress. These are interstate commerce problems that simply cannot be addressed by the individual states.

Federal antitrust laws work well to remedy problems in mature markets. But they are not well suited to guide the transition to competition for industries, such as the electric utility industry, that start from highly concentrated monopolies. Antitrust laws alone cannot convert such industries to ones that are capable of being controlled by competitive forces. Our antitrust laws are very useful tools to address market power problems after they have been identified. But they are not particularly useful in identifying and rooting out the causes of these problems.

The identification of such problems in any modern industry is hard, but in the electric utility industry, this is not simply hard, it is extremely difficult. Electricity is a real time product. It is literally consumed as it is produced. It cannot be stored. This makes transactions in the electricity market very vulnerable to subtle discriminations such as capacity reservations on existing transmission facilities and manipulation of such seemingly innocuous events as unscheduled maintenance of strategically located generation and transmission facilities. For these reasons, the antitrust agencies have generally favored structural remedies. And have testified before this subcommittee in that regard.

Congress held out the promise of competitive wholesale electric markets when it enacted the Energy Policy Act of 1992. This promise was reaffirmed when the Act was implemented aggressively by the Federal Energy Regulatory Commission. But FERC has now acknowledged that its approach, reflected in Order 888, is deficient in many respects. Its current proceeding on regional transmission organizations is an attempt to address some of these deficiencies. Other deficiencies are apparent as well, including the absence of solid, clear legal authority under which FERC can effectively remove obstacles in the interstate commerce of electricity. Only Congress can address these problems.

Congress should also act to ensure the reliability of the electric utility system. Voluntary reliability standards are no longer adequate. In this area, at least, there is a consensus among all of the stakeholders that Congressional action is required, even though some disagreements still persist with respect to the role of the states and state utility commissions.

And finally, Congress must act to address U.S. Tax Code provisions that are inconsistent with the new utility environment being brought about by state restructuring legislation. Public power's "private use" problem is a clear example of this. The operational limits imposed on publicly owned utilities with facilities financed by tax-exempt bonds by statutory private use requirements are simply incompatible with the demands of the new market. These limits must be removed.

WHAT SHOULD BE INCLUDED IN FEDERAL RESTRUCTURING LEGISLATION?

From APPA's perspective, the following essential elements should be included in Federal restructuring legislation:

- Provisions that clarify federal law to ensure that FERC has jurisdiction to enforce comparability in transmission services on facilities that are in fact part of the national grid.
- Provisions that broaden the criteria used by FERC in the review of proposed mergers, expand the authority of FERC to review holding company to holding company mergers, transmission company mergers, and significant sales of generation assets, and enable the Commission to address market power problems by means up to and including asset divestiture.
- Provisions that expand the authority of FERC with respect to the creation of regional transmission organizations that are truly independent, and sufficiently broad in scope and configuration to promote efficient and non-discriminatory power markets, while taking into account the specific, unique characteristics, rights and obligations of publicly owned utilities.
- Provisions to address "tax transition" problems arising because provisions of the U.S. Tax Code are out of sync with state restructuring legislation.

With the exception of the last item, H.R. 2944 falls far short of what must be included in Federal legislation. For this reason, APPA opposes H.R. 2944 in its present form.

We are well aware that what we believe must be included in Federal legislation is seen by some as an expansion of regulation that is incompatible with deregulation and creation of an open, competitive market. APPA disagrees. Expanded regulation in some areas is in fact a prerequisite to expanded competition in others. As Albert Foer observed in the article to which I previously referred:

> Experience with examples of deregulation teaches that competitive markets do not materialize just because theoreticians believe they are good or because there are basic economic characteristics of a market that make it possible to perform more efficiently. Rather, competitive markets are deeply embedded in social, intellectual, legal, and political institutions. Transitions from regulation to competition, therefore, are not likely to work out very well unless the institutional framework is also being changed in parallel ways. Transitional problems must not be dismissed as if they don't affect future institutional relationships. The transition can create a life of its own, leading to outcomes that were never envisioned.

We are extremely concerned over the institutional framework that is currently evolving, unchecked for the most part by either FERC or the states. Expanded regulation in the areas identified above are absolutely essential through this transition period to put in place the right institutional framework that will carry us from regulated, vertically integrated monopolies of today, to the deregulation of the bulk power market tomorrow.

That expanded regulation in some areas is not only compatible with but essential for competition in others is obvious from a review of the transmission access provisions of the Energy Policy Act of 1992. Congress correctly concluded that competition in the bulk power market could not occur unless it expanded the authority of the Federal Energy Regulatory Commission in the regulation of interstate transmission facilities. Congress had the wisdom to understand that expanded regulation was required to promote competition in the bulk power markets. We hope Congress demonstrates the same wisdom today, and takes the steps necessary to ensure that the promise of competition it held out in 1992, becomes a reality as we move into the next millennium.

COMMENTS ON H.R.2944

H.R. 2944 is a lengthy and complex piece of legislation. We are still reviewing its provisions to determine their ultimate effect. However, we have set forth below our concerns with respect to several parts of this legislation, together with recommended changes. Our comments are not organized in the order of their priority to public power. Instead, they follow the order in which these issues arise in H.R. 2944.

Section 101—Clarification of State authority regarding retail electric competition; clarification of Federal and State jurisdiction.

APPA believes that the States and the self-regulated publicly owned utilities should retain the authority to decide if, when and how to go to retail competition. The legislation preserves these rights. However, in attempting to create a bright line distinguishing Federal and State regulatory jurisdiction, two provisions of H.R. 2944 combine to eviscerate FERC jurisdiction over significant components of the interstate transmission network.

Section 101(b)(1)(B) does not allow FERC regulation over bundled retail sales of electric energy. Section 101(e) allows for a FERC determination of whether a par-

ticular facility qualifies as transmission or distribution, but requires FERC to give deference to State commission decisions. When these provisions are combined, this section cuts FERC out of the regulation of significant amounts of transmission access and use over bundled sales. If this section is interpreted to allow a preference for bundled firm load over unbundled firm load on the same transmission system under emergency situations, then it is clearly inappropriate. Such an interpretation would undermine the goals of promoting competition and standardizing regulation of the national grid.

To avoid FERC regulation and to frustrate effective competition in the bulk power market, investor owned utilities are hard at work "refunctionalizing" their assets. What was transmission and therefore subject to FERC jurisdiction yesterday, is being redefined or refunctionalized as distribution, putting those facilities under state commission jurisdiction in order to evade FERC regulation tomorrow. As noted in a paper written by Whitfield A. Russell, president, Whitfield Russell Associates, "Refunctionalization of Transmission Assets Under FERC Order 888: Impact on Market Power," "refunctionalization presents an opportunity for transmission owners to charge vastly different rates (and to offer delivery services on vastly different terms and conditions) to similarly situated retail and wholesale customers (both generators and consumers)." (A copy of Mr. Russell's paper is attached to this testimony.)

APPA members have witnessed this refunctionalization trend as well. Roy Thilly, the current president of APPA and the Chief Executive Officer of Wisconsin Public Power, Inc., in testimony at a workshop on market power and consumer protection sponsored by the Federal Trade Commission on September 13, 1999, stated that "one Wisconsin utility has asked our PSC to find that there is virtually no transmission in our state. This utility would refunctionalize more than 80% of its transmission system to distribution, gutting its obligation to transfer control to an ISO." The objective of this action, according to Mr. Thilly, is clear. It is "to avoid giving up control and to create an anticompetitive buffer between customers and the market."

APPA supports the "function" approach in H.R. 2944 (and FERC Order No. 888) to determine which facilities are part of the transmission network and therefore subject to FERC jurisdiction, and exclude facilities that constitute part of the distribution network. However, the process must be carefully and consistently administered to ensure that it does not permit abusive refunctionalization actions. While it may be appropriate for FERC to give "due consideration" to State commission determinations regarding the function and purpose of specific transmission facilities, requiring that they defer to these determinations is extremely problematic. We urge the subcommittee to amend section 101(e) by substituting "due consideration" for "due deference."

Section 102—Open Access for all Transmitting Utilities.

Public power systems own approximately 8% of transmission facilities at voltage levels of 138kV or higher. These facilities are widely dispersed across more than 100 public power systems, and most of these facilities are not part of the backbone transmission grid but are an instead part of local distribution networks. For the most part, those publicly owned utilities that own significant transmission facilities that constitute part of the interconnected grid have voluntarily filed open access tariffs. We believe it is difficult on public policy grounds to sustain the proposition that publicly owned transmission facilities should be subject to FERC jurisdiction. Such Federal preemption of local authority in order to regulate a very limited amount of transmission when the owners of those facilities are already providing comparable service appears to us to be a solution in search of a problem.

We are pleased that H.R. 2944 proposes to minimize the expansion of FERC jurisdiction over publicly owned transmission facilities by permitting FERC to waive jurisdiction over transmitting utilities whose transmission facilities are "limited and discrete" and "do not form an integrated grid," and for "small" publicly owned transmitting utilities (annual sales of 4 million megawatt hours or less) that are "not part of a centrally dispatched power pool."

Presumably, the objective of expanding FERC jurisdiction over publicly owned transmitting utilities is to ensure that the transmission services they provide to third parties are comparable to the services they provide themselves. We believe that this objective can be achieved by limiting FERC jurisdiction to the non-rate terms and conditions of service for publicly owned transmitting utilities that do not obtain a FERC waiver. FERC jurisdiction over rates of publicly owned transmitting utilities could conflict with the responsibilities of those utilities to abide by revenue requirements contained in their bond covenants, and could also conflict with state legal and constitutional requirements.

APPA recommends that FERC jurisdiction over public power systems that do not obtain waivers should be limited to non-rate terms and conditions to ensure they are comparable to the transmission services that private power companies are required to offer under their open access tariffs. FERC jurisdiction over rates and revenue requirements for public power systems should be limited to ensure comparability. Where FERC determines that rates are not comparable or are discriminatory, it could remand the rate to the local regulatory authority for review and revision as necessary. Public power systems would therefore retain local control over rate making and revenue requirement decisions.

Section 103— Regional Transmission Organizations

The Regional Transmission Organization (RTO) provision is designed to ensure that every transmitting utility will be in a RTO by 2003. This is a positive step, but there are serious problems with the timing, conditions for FERC approval, and the absence of FERC authority to correct problems after the RTO deadline passes.

APPA continues to support the authority of FERC to establish and require utility participation in strong, truly independent RTOs in order to facilitate the development of vigorously competitive regional power markets. The legislation should provide such authority as well as appropriate criteria to govern its use. In addition to such issues as independence, size and scope of RTOs, the statutory criteria should accommodate the unique characteristics and legal requirements of public power to ensure that public power's participation by FERC order is not inconsistent with state laws and constitutional requirements. Furthermore, the additional criteria for public power participation must be consistent with bond covenant requirements and not impair control of local system operations or reliable and economic service to the public served by publicly owned facilities for whose benefits public funds have been expended. Lastly, the criteria should not require public power systems to participate in certain ISOs or RTOs in cases where they have been mandated as part of state legislation to promote retail competition and such legislation has preserved the right of public power systems to determine whether or not to join such entities.

The deadlines established, filings by January 1, 2002, participation by January 1, 2003, will delay by at least two years the current rulemaking actions of FERC (Docket No. RM99-2-000) to promote an open and more competitive bulk power market through the creation of RTOs. FERC proposes that all public utilities that own, operate or control interstate transmission file proposals for an RTO by October 15, 2000, and that RTOs be operational by December 15, 2001, more than a year earlier than required under H.R. 2944. This delay is totally unnecessary. But it is inconsequential when one considers the opportunity for additional delays in the creation of RTOs provided by this legislation. If enacted in its present form, H.R. 2944 will delay the formation and effective operation of RTOs for several years beyond 2003. Section 103 requires that a stay be issued whenever a FERC RTO order is challenged through a petition for rehearing before the Commission, or subsequently is challenged in court.

We urge the subcommittee to consider carefully the consequences of this provision of H.R. 2944. Consider, for example, what would have occurred if FERC had been required to stay the implementation of Orders 888 and 889. These orders were issued in April, 1996. Petitions for rehearing were filed, granted by FERC, and certain modifications were made in the initial orders. Thereafter, these orders were challenged in an appeal that is now pending before the U.S. Circuit Court of Appeals for the D.C. Circuit. The case has not yet been argued. It is extremely complex, with multiple parties. No decision is expected until at least the fall of 2000. Then, of course, there is the possibility of Supreme Court review and/or a remand to FERC for reconsideration of specific issues. If Congress had directed that these orders must be stayed pending appeals, we would not yet have seen even the limited progress toward more competitive bulk power markets that these orders have brought about.

Under current law, the Commission has the discretion to stay its orders during appeal. We believe it should retain this discretionary authority with respect to RTO orders. APPA also recommends that the deadlines proposed for RTO filings and formation should be reconsidered. Deadlines give comfort to those seeking to delay the process, and the prospect of mandatory stays of FERC orders provides a potent weapon for those determined to frustrate the creation of RTOs.

Even more troubling than these timing problems, however, are the criteria established for FERC consideration of proposed RTOs. There are several characteristics that must be part of any RTO. It must be independent to ensure that those who control transmission cannot exercise vertical market power. It must have boundaries that are rational, and that prevent the balkanization and gerrymandering of the grid. It must take into consideration the needs of all stakeholders, including,

the needs of public power transmitting utilities, to ensure fair and equitable treatment of all. In addition, while it may be appropriate for FERC to provide incentives for *performance*, it is not appropriate for FERC to provide incentives for *participation*. And finally, it is absolutely essential to clarify FERC's legal authority to accomplish these objectives, and to order the creation or reconfiguration of RTOs, consistent with the characteristics set forth above, if the proposals brought forward do not achieve at the outset, or over a reasonable period of time, the desired results. Section 103 is deficient in all of these areas.

APPA notes the following deficiencies and problems with the provisions of section 103 of H.R. 2944 (set forth in the order in which they appear in this section and not necessarily in their order of importance to APPA):

- FERC is directed to approve an RTO application filed by a single transmitting utility if it meets certain criteria. Given the massive consolidation occurring through mergers and acquisitions, single utility RTO proposals are a distinct possibility. The proposed criteria do not require the effective broad participation of all affected stakeholders, particularly wholesale customers. The absence of substantial customer support for a RTO filing indicates that the RTO business plan reflects monopoly needs, not market needs.
- The Commission may approve proposals that do not meet all standards but are consistent with such standards. Since the Commission cannot order the creation of RTOs, it may feel compelled to accept proposals that do not fully satisfy those conditions and therefore will not effectively promote the development of a more competitive bulk power market. Further, this is an invitation to delay through litigation over what constitutes substantial compliance. Since FERC cannot order participation in a RTO that is not of the transmitting utility's choice, and a finding of non-compliance must be stayed through the appeals process, utilities determined to prolong the RTO creation process have every opportunity to do so. Clearly, this will result in the failure of this legislation to achieve the desired results of RTO creation and participation in a timely fashion.
- The "independence" standard will not produce RTOs that are in fact independent of market participant control over operations. Permitting passive ownership interests, and ownership of ten percent of voting interest (page 20, lines 2 through 16) must be deleted. So-called "passive" ownership is not innocuous. In filings in FERC Docket No. RM99-2-000, the Edison Electric Institute concedes that a "passive" ownership carries with it a fiduciary relationship to the passive owners. The management and board of for-profit transcos will be fully aware of the impact of their decisions on the generation interests of the "passive" owners. There will be an inherent conflict of interest with respect to decisions related to unaffiliated generation assets that compete head-on with the generation interests of the transco's "passive" owners. A ten percent voting interest in a company with widely held stock would essentially permit the ten percent owner to control corporate affairs. Two private power companies, each with ten percent voting interest, would clearly permit those two companies to control the corporation. APPA is opposed to the ownership provisions that purportedly qualify but in fact undermine the independence standard. The legislation should be silent in this regard and permit the Commission to decide (and if necessary reconsider) what is permissible in terms of both passive ownership and voting interests.
- The conditions regarding scope and configuration are appropriate, but are problematic when considered from public power's perspective. Given the limited amount of transmission facilities owned by publicly owned utilities, it will be difficult if not impossible for them to develop, on their own, RTOs that "comprise an appropriate scope and regional configuration." Of necessity, they will be forced to participate in RTOs constructed by (and perhaps with passive ownership and controlling voting interests held by) investor owned utilities. There is no requirement that a collaborative process be established that will protect the rights of these systems. Indeed, there is no guarantee against (and based on past practice every reason to be fearful of) RTO proposals developed by private power companies that: operate against the interests of public power; do not accommodate public power's unique characteristics and legal requirements; may be inconsistent with state laws and constitutional requirements under which public power systems operate; are not consistent with public power's bond covenants; and impair public power's control over local systems operations or their ability to provide reliable and economic service to the public served by them and for whose benefit public funds have been expended to develop publicly owned facilities. Finally, to comply with this legislative directive, some public power systems may be faced with the unreasonable choice of submitting a proposal to FERC to join what amounts to a RTO created by state legislation to promote

retail competition where that same state legislation has reserved to them the right to decide whether or not to participate. In those cases, FERC approval could amount to a Commission directive changing a RTO approved by the Commission prior to enactment of this legislation, something expressly prohibited in the legislation itself.

- Incentive transmission pricing policies to promote RTO formation are expressly authorized, and such incentive prices are to be extended to participants in existing RTOs. APPA strenuously opposes rate incentives, performance based rates, and relaxed FERC regulation offered as inducements to public utilities to participate in RTOs. Incentives should only be provided for performance, not participation.
- The Commission is permitted to withdraw approval previously granted if the RTO fails to comply with provisions of the legislation. But what happens then? The Commission is expressly prohibited from requiring utilities from participating in a different RTO than the one it proposes. It is absolutely essential that this deficiency be recognized and addressed.
- Finally, this section in combination with other provisions of the legislation that will contract the scope of FERC jurisdiction over facilities that are in fact part of the integrated transmission grid, is likely to produce entities that are RTOs in name only, but without much of a functional transmission grid to actually administer.

In 1978, when Congress was considering President Carter's National Energy Policy Act, it came close to expanding FERC authority to require transmitting utilities to provide open access. In the end, Congress acceded to the pressure of private power companies, and the authority given to FERC was so encumbered with unreasonable and unrealistic conditions that the authority presumably granted to the Commission could never be exercised. This mistake was finally corrected 14 years later as part of the Energy Policy Act of 1992. We fear that the same fate, and failure, will occur with respect to the creation of RTOs under this section. This provision will not get the job done. The RTO proposals brought forth by private power companies if this provision is enacted will not promote competition. Instead, they will further entrench the control over transmission in the hands of a relatively few, very large private power companies. Wholesale customers, retail customers in states that have opened their markets, and independent power producers will suffer. If the past is prologue, it will be at least a decade before Congress returns to this issue and finally takes the steps necessary to create the RTOs or other grid management institutions required to ensure that all industry participants have full, fair and nondiscriminatory access to interstate transmission facilities.

Title II—Reliability

It is important at the outset to reflect on the ultimate goal of uniform reliability standards to govern interstate commerce in electric transactions. First, electricity is too important to our society to permit voluntary reliability standards for individual utilities, that may or may not be followed depending on the economic consequences of any particular opportunity. And second, our society simply cannot permit the existence of inconsistent rules governing the real-time operation of the interstate bulk power market. Uniform rules, applicable to all, that can be enforced, are essential.

APPA has been an active participant in the construction of industry consensus language contained in Title II that establishes an independent, industry self-regulatory electric reliability organization, transitioning the present North American Electric Reliability Council (NERC) to the North American Electric Reliability Organization (NAERO), to ensure the continued reliability of the interstate high-voltage transmission grid. We were also signatories to the recent letter to Chairman Barton that expressed concern with the specific language of the proposal put forth by the National Association of Regulatory Utility Commissioners (NARUC) regarding a state savings clause. We note that H.R. 2944 has included language that creates a state savings clause related to the reliability of local distribution facilities. As noted previously, through refunctionalization the relatively limited facilities that are today identified as distribution facilities can be greatly expanded to include facilities that are in fact part of the interconnected grid. If this is permitted to occur, the significant benefits anticipated from the enactment of the reliability provisions in H.R. 2944 will be diminished. We look forward to continuing to work with the state entities and the Subcommittee to develop language that reasonably addresses these legitimate state concerns in a manner consistent with the intent of the placing of responsibility for bulk power system reliability in the hands of a self-regulating reliability organization.

Title III—Consumer Protection

These sections guard against unfair trade practices and are generally consistent with APPA policy related to consumer protection. However, protecting consumers from abuses in a competitive market assumes the existence of such a market. That assumption is highly suspect in the current environment, and unlikely to change under the environment that would be created if H.R. 2944 is enacted without significant modification. APPA supports strong consumer protection provisions, but we believe that the most significant protections Congress can provide consumers is the creation of an industry structure that will in fact create a competitive market. We believe we can put considerable trust in a truly competitive market. But we do not have such a market at present. We do not believe such a market will arise under the laws as they now exist, and we are even more skeptical that they will arise under the laws as they are proposed to be restructured and revised by H.R. 2944.

Title IV—Mergers

Section 401—Electric Company Mergers and Disposition of Property.

APPA strongly opposes the changes regarding the authority of FERC with respect to its review and approval of mergers and asset disposition. We cannot support this legislation unless FERC's current authority to review mergers through full evidentiary proceedings is not only preserved but expanded to address both existing and incipient market power problems.

Under existing law, FERC must approve disposition of certain assets (which may or may not include generation facilities) by "public utilities" after "notice and opportunity for a hearing" if the proposed disposition is "consistent with the public interest." The first draft of this legislation proposed to eliminate FERC's authority in this area entirely. H.R. 2944 is an improvement over the draft proposal in that it preserves this authority, clarifies the uncertainties regarding FERC jurisdiction over the transfer of generation assets, extends jurisdiction to include holding company systems that include electric utility companies, and requires consideration of the effect of such transfers on competition in wholesale and retail markets. Expanding the reach of the Commission is absolutely essential, and requiring consideration of the effects on competition of such transfers is an improvement over the provisions of existing law.

Unfortunately, these improvements are more than offset by the prohibition of on-the-record evidentiary hearings. Under current law, FERC has the discretion to utilize both "paper" hearings with or without an opportunity for oral comments, or on-the-record evidentiary proceedings, depending on complexities of each specific case. H.R. 2944 would eliminate the option of evidentiary hearings. Instead, those challenging a proposed merger or other disposition of assets, would have 60 days within which to file written and oral comments. FERC would then have 90 days (and up to an additional 90 days) to issue its order. Existing law, deficient as it is, is far better than what is proposed in H.R.2944.

If Congress truly intends to protect all electric consumers from abuses of market power, it must first preserve the procedural protections of the review process by not eliminating the opportunity for evidentiary proceeds, second, expand the types of transactions subject to FERC review, and third, expand the scope of the Commission's review to require consideration of how proposed mergers and acquisitions will affect wholesale and retail competition. Further, in reviewing mergers, FERC should be directed to employ a "net positive benefit test," not simply the "no net harm" test currently utilized. Unless proposals brought before FERC actually produce net positive benefits and enhance competition, they should be rejected.

Finally, FERC's authority to address existing market power problems must be expanded. Concentration of market power in generation is already a problem, and likely to become an even greater problem in the near future. For the past several years, we have had a surplus of generation. That surplus is quickly disappearing nationally, and has already disappeared in some regions. At the same time, some industry participants have been able to acquire vast amounts of generation resources, and through these acquisitions they will be able to exercise generation market power in the future.

APPA believes that these problems can only be addressed by providing FERC with additional authority to deal with generation market power. Generation market power may well be a transition issue. This would certainly be the case if we are able to achieve, through federal legislation, large, regional and totally independent grids that are able to remove constraints through the construction of additional transmission. This, combined with ease of entry into the generation markets, may eliminate, over the long term, generation market power.

However our starting point is one of high degrees of generation concentration in specific markets that also have significant transmission constraints. The consequence of these two factors is higher prices and poorer service for consumers. What is required is clear authority for FERC to deal quickly and effectively with the exercise of generation market power.

Remedies here can be temporary, not permanent. They need not have a long term impact on the ownership or control of utility assets. However, they should address the temporary market distortions. For example, "temporary" divestiture of generation could occur through an auction procedure for capacity for limited periods of time. Or FERC might impose cost-based rates for generation where market power exists. What is required is to transform FERC from an arcane price-setting agency to an agency with an affirmative duty to structure and oversee the bulk power market to ensure that it will be effective and sustain competition over time. APPA recommends that FERC be provided with a "toolbox" of potential remedies to deal with generation market power. The toolbox should include the ultimate tool of divestiture authority. Just as the hangman's noose truly focus the attention of the condemned, the prospect of mandatory divestiture as a last resort to address generation market power would focus the attention of those with generation market power. Perhaps it will never be used. But having it available in the "toolbox" is essential. After a reasonable transition period, FERC could be directed to report to Congress. Such a report should include whether transmission organizations have captured the proper geographic scope, whether they are competitively neutral, and whether they provide for effective competition markets throughout the country. When these conditions are met, generation market problems may well have been effectively addressed, and the "tools" placed in the FERC "toolbox" might then be removed.

Section 402—Elimination of Review by The Nuclear Regulatory Commission

APPA was the leading proponent of Congressional enactment of Section 105 of the Atomic Energy Act. With the exception of the transmission access provisions of the Energy Policy Act of 1992, this provision of law has done more to open transmission access to wholesale customers than any other act of Congress, including the antitrust laws.

Today, many private utility owners of nuclear facilities are selling or proposing to sell these assets to a few domestic and Foreign corporations. These nuclear facilities are large—ranging from several hundred to over one thousand megawatts of capacity. Collectively, nuclear facilities provide nearly 15 percent of the total generation capacity available in the United States.

As operating licenses for these facilities are transferred from incumbent owners to an ever decreasing number of domestic and Foreign operators, an evaluation of whether such transfers will create or maintain situations inconsistent with the antitrust laws seems more, not less, relevant. Repealing the antitrust review authority of the NRC, combined with other aspects of H.R. 2944, will contribute to the consolidation and abuse of market power in the hands of a few entities. As the initial advocate of this provision of law, and consistent with APPA's concerns over the total absence of effective controls of market power in H.R. 2944, APPA objects to this section.

While we object to the repeal of this provision of consumer protection legislation, we believe that conditions previously imposed in reviewing the antitrust consequences of granting construction permits and operating licenses for nuclear power generation facilities must be enforced. H.R. 2944 preserves these conditions, and their enforcement. While we strongly object to the repeal of this provision of law, if that were to occur, conditions previously imposed must be preserved and enforced.

Title V—Promoting Competition

Section 501—Retail Reciprocity

APPA has no policy on this provision but urge further consideration. Presumably, the reciprocity requirements that prohibit utilities that do not provide retail customer choice in their own service areas from engaging in retail markets where choice is permitted, are intended to promote competition. However, this provision could actually limit the number of competitors in a particular market, thereby producing the opposite of what is intended. As a practical matter, these requirement can be easily avoided if utilities prohibited from dealing directly in another state work through a power marketer that is not so limited. If this is not an option, the reciprocity requirements might operate as a backdoor mandate for retail competition. For all of these reasons, we suggest that this provision be reconsidered.

Subtitle B—Public Utility Holding Company Act of 1935

The Public Utility Holding Company Act of 1935 has been more important than any other Act of Congress in regulating the structure of the electric utility industry. Unlike other regulatory statutes, the Holding Company Act requirements are passive. It defines permissible structures of holding company formation in order to ensure effective state and federal regulation of electric utility holding companies, and it does so in an attempt to protect consumers, investors and the public interest. This statute has been an outstanding success. Its repeal or modification should be considered with great caution.

APPA opposes repeal of the Holding Company Act on a stand-alone basis, that is, outside of the framework of comprehensive, industry restructuring legislation. However, APPA will not object to repeal of PUHCA, provided that repeal is coupled with strong market power provisions. Such provisions are not included in H.R. 2944, and therefore APPA opposes PUHCA repeal as proposed in this legislation.

More acceptable to APPA than the provisions of H.R. 2944 are proposals in other legislation pending before this Congress that provide for prospective repeal in 18 months from enactment, not the 12 month period contained in this legislation. APPA is also concerned that H.R. 2944 restricts regulatory access to books and records of holding companies to review only costs incurred, as opposed to permitting a broader review of total operations. We believe this restriction is inadequate to protect the consumer interest. Further, not only are adequate consumer protection provisions lacking in this section of the bill, but the weakening of market power protections throughout the legislation make the repeal of PUHCA unacceptable even though it would occur as part of broader comprehensive restructuring legislation.

Section 541—Aggregation

This section authorizes entities, including political subdivisions within a state, to aggregate consumer electric needs. We strongly support this provision and urge that it be preserved in any legislation adopted by this subcommittee. One consistent concern of residential consumers across the country is that they will be shut out of the benefits of competition. Noted economist and one of the fathers of deregulation in this country, Alfred Kahn, in a recent speech at an EEI-sponsored meeting in Chicago, stated that he sees few signs that the deregulation of the electric utility industry will provide benefits for small customers any time in the near future. Aggregation, particularly of small consumers, provides a solid, consumer-oriented tool that could provide options for residential and small business customers. APPA supports this provision so long as it expressly preserves the rights of states and political subdivisions to aggregate the electric needs of their citizens.

Title VI—Federal Electric Utilities

More than a quarter of APPA members purchase power from the Tennessee Valley Authority and the various Federal power marketing administrations. We support regionally-based solutions that address the unique characteristics and relationships that TVA and the Federal power agencies have with their wholesale customers. The provisions in this section are generally consistent with the goals of APPA policy for maintaining the existing TVA and PMA structure as closely as possible with current law. With respect specifically to the Federal power marketing administrations, we do not believe that legislation is necessary to maintain the current cost-based rate structure. In fact, including such language in the legislation raises questions regarding cost-based rates for these entities, and provides opportunities for opponents of the Federal power program to advance proposals to change the cost structure of these agencies from cost-based to market based rates. For these reasons, APPA supports deleting the PMA sections dealing with PMA rates altogether. Inclusion of language that simply restates current practices only invites amendments to change such practices.

Title VII—Environmental Provisions

Existing law providing incentives for public power investment in renewable energy must be maintained and enhanced. H.R. 2944 preserves the Renewable Energy Production Incentive Program (REPI), and restricts it to public power systems and other non-profit developers of renewable energy. Even though this provision is little more than a reaffirmation of existing law, APPA supports this aspect of the legislation. However, the legislation would and should not exclude landfill methane gas recovery from eligible biomass projects.

APPA believes that increased use of available resources can be best achieved through competitively neutral incentives that treat public power entities on an equivalent basis as non-public power entities. Incentives should be structured to assist power generating entities to overcome existing barriers to increased renewable

energy use and deployment of other green technologies. Incentives should be structured to provide comparable benefits to each region of the country and allow power generating entities to be most responsive to the needs and preferences of their customers and the competitive market. The incentives should be easy to administer and provide sufficient documentation for easy verification. To the extent REPI is retained, it should be changed to address the uncertainty of annual congressional appropriations and funding.

APPA proposes a two-prong approach to encouraging renewable energy development in the public power community. The first is to address the existing authorized REPI program by providing funding to cover current project recipients. Under law, REPI participants are eligible for ten-year payments calculated at 1.5 cents per kWh of electricity generated from eligible projects. We propose that Congress direct DOE to make current REPI project sponsors whole, and that sufficient funds be allocated to cover all eligible projects. Funds could be allocated by any number of mechanisms including: 1) one-time lump sum appropriation; 2) creation of a trust fund/escrow account funded at a level sufficient to allow the revenues to grow over time to cover project costs; or 3) accelerated appropriations to provide advance funding for future REPI payments, similar to the Clean Coal Program.

Part two of the package involves the creation of new incentives available to non-taxpaying entities that do not participate in the revised REPI program. The option we prefer is the creation of refundable production tax credits under the Treasury Department that could be exchanged with other utilities. Non-taxpaying entities would be eligible to claim a tax credit similar to the Section 45 credit. Specifically, the amount of credit is not effected by the amount of federal tax liability, rather, it would be calculated along the same guidelines as the Sec. 45 and REPI projects. As with these two programs, a participant would be given a refund based on a 1.5 cents (adjusted for inflation) per kWh of electricity generated from renewable energy projects.

Title VIII—Tax Provisions

While APPA appreciates the fact that H.R.2944 maintains the structure or H.R.721 as the appropriate means to resolve public power's "private use" problem that has arisen from the current incompatibility of U.S. tax laws and state restructuring demands, we are very concerned that what has been included in H.R. 2944 modifies provisions of H.R. 721 in a few significant ways. H.R. 721 has been carefully crafted to address public power's private use problem with full consideration of the interests and concerns of all market participants. H.R. 721 has been co-sponsored by more than 85 members of the House of Representatives, from both political parties spanning the broad reach of the political and ideological spectrum.

H.R. 2944 incorporates the major elements of H.R. 721 but restricts the legitimate use of tax-exempt financing by publicly owned utilities for certain purposes in the future beyond the restrictions already contained in H.R. 721. At the same time, H.R. 2944 proposes to vastly expand the tax subsidies available to investor owned utilities with respect to nuclear decommissioning expenses and the tax treatment of decommissioning funds in event of sale of nuclear facilities. The provisions relating to nuclear decommissioning expenses not only go far beyond what has been proposed by the Administration, but go beyond provisions found appropriate by the House Ways and Means Committee and included in tax reform legislation enacted by Congress before the August recess and recently vetoed by President Clinton. This lack of symmetry in treatment of public and private power tax issues is troubling.

These "tax transition" issues are not within the jurisdiction of the House Commerce Committee. Because they are obviously part of the electric utility restructuring debate, and because members of Congress will look to members of this subcommittee and the full committee for guidance on how all of these restructuring issues should be addressed, we are very pleased that for the most part H.R. 721 was incorporated in H.R. 2944. Their inclusion in H.R. 2944 sends a strong signal to committees of jurisdiction regarding the preferred approach to dealing with these matters. We appreciate Chairman Barton's desire to reconcile the tax code problems, and his desire to address the private use problem using the basic framework of H.R. 721.

The provisions of H.R. 721 are an extremely fair and reasonable resolution of public power's private use problem. APPA insists that this problem be addressed. Unless we are convinced that this problem will be addressed, and that it will be addressed in a fair and equitable manner either as part of comprehensive restructuring legislation, or on a stand-alone basis, we will strongly oppose any federal electric utility restructuring legislation.

Conclusion

APPA supports comprehensive Federal legislation to promote competition in the electric utility industry. H.R. 2944 in its present form will not achieve this goal. It fails to address serious market power problems. It is a step backward in its treatment of FERC review of utility mergers and the further accumulation of market power by private power companies. It purports to establish Regional Transmission Organizations. But the promises it holds for the creation of truly independent, broad RTOs that will promote competition in the bulk power market cannot possibly be met given the criteria established for their approval by FERC, and the absence of real authority for FERC to help structure the industry in ways that will promote competition and benefit consumers.

APPA opposes H.R. 2944 in its present form. At the same time, APPA wants Congress to enact legislation that promotes competition and ensures that the benefits of competition—lower rates and better service—will be experienced by all electric consumers. APPA will continue to work with Congress to achieve these results.

Mr. BARTON. Thank you very much.

Next we will hear from Mr. David Owens, executive vice president of Edison Electric Institute.

Your full statement is submitted for the record and you have 6 minutes. Welcome.

STATEMENT OF DAVID K. OWENS

Mr. OWENS. Thank you, Mr. Chairman.

Good morning, Mr. Chairman and members of the subcommittee.

EEI supports Federal legislation that removes Federal barriers to competition, facilitates State restructuring actions, addresses critical transmission and reliability issues, and applies the same rules to all competitors.

We believe that H.R. 2944 makes significant progress toward achieving some of these goals. On others we have some concerns and suggestions.

My written testimony outlines EEI's views on specific provisions, so I will just mention a few highlights for you.

We commend the chairman for removing Federal barriers to competition by removing PUHCA and reforming PURPA. In addition, the bill addresses a number of important transmission and reliability issues. For example, it would establish a self-regulating reliability organization and extend FERC transmission jurisdiction over all transmission facilities. We certainly believe that is an important step in the right direction.

We also commend the chairman for recognizing that expansion of transmission capacity is critical. However, the bill's provisions, unfortunately, do not achieve this important goal. Similarly, the bill recognizes the need to expedite FERC's merger review, but, at the same time, the merger provisions would result in more government regulation.

We are concerned with some key areas of H.R. 2944. First, the bill fails to develop the same rules for all competitors. It would allow, for example, Federal utilities, government-owned utilities, and co-ops to use their current subsidies to construct new generation of transmission facilities in a competitive market. This would simply give these entities a tremendous advantage over their competitors.

Simply put, the market would follow the subsidies, and government share of the electricity market undoubtedly would increase.

Second, the bill would reregulate, not deregulate, in several areas.

H.R. 2944 would expand Federal regulation by establishing a deadline for the formation of regional transmission organizations and by increasing FERC's merger authority.

Electricity markets are robust today. Given the degree of remaining Federal and State regulation, we believe neither of these provisions is necessary or desirable.

Third, the bill would intrude into State jurisdiction over retail electric service on a number of issues, including interconnection standards, net metering, aggregation, and retail reciprocity.

As members of this subcommittee well know, 23 States are moving forward with their own restructuring plans. They certainly should not be forced to revisit key provisions.

Similarly, the remaining States are considering their own plans, and they certainly want their flexibility to maintain the development of these areas.

We look forward to working with the chairman and other members of the subcommittee to improve these areas of the bill.

Finally, we commend the chairman for not making H.R. 2944 a vehicle for micro-managing competition with punitive market restrictions. You heard some of those from Mr. Richardson.

We are pleased that the bill does not expand FERC authority to order utility divestiture, nor does it impose competitive handicaps on utilities and their affiliates.

Proponents of punitive market restrictions claim there are not enough competitors in the market. Nothing could be farther from the truth. There are thousands of electricity suppliers already in the marketplace, plus big, well-known, national companies, including some of the world's large oil and gas companies. They are certainly very active in this market.

Proponents of punitive market restrictions also claim that competitors will not be able to reach consumers. They ignore the continued tight Federal and State regulation of essential utility facilities. These are the transmission lines which will ensure all competitors nondiscriminatory access to utilities' wires. And they ignore the continued State regulation of the utility affiliate transactions.

The ability to bring lower prices or better service to consumers is what competitive markets are all about. Market share, alone, simply does not equal market power. Suppliers cannot be equalized in competitive markets. As long as there is nondiscriminatory, open access to provide consumers with a choice of suppliers and no company can manipulate prices or shut others from the marketplace, consumers will find the best combination of price and services to meet their needs.

As I have stated, EEI strongly believes that H.R. 2944 makes significant progress toward achieving important public policy goals, while falling short on others.

We commend the chairman for his efforts to develop a workable electricity bill. We look forward to continuing to work with him and members of this committee.

Thank you for this opportunity to provide our views. I certainly look forward to your important questions.

[The prepared statement of David K. Owens follows:]

PREPARED STATEMENT OF DAVID K. OWENS, EXECUTIVE VICE PRESIDENT, EDISON ELECTRIC INSTITUTE

INTRODUCTION

I am David K. Owens, Executive Vice President of the Edison Electric Institute (EEI). EEI is the association of U.S. shareholder-owned electric utilities and industry affiliates and associates worldwide. A super-majority of EEI's members have established EEI's approach to competition in the electricity industry, although a few members disagree with some elements of that approach. We are pleased to have the opportunity to testify before the Subcommittee on H.R. 2944, the Electricity Competition and Reliability Act.

EEI supports federal electricity legislation that removes federal barriers to competition, facilitates state restructuring actions, addresses critical transmission and reliability issues and applies the same rules to all competitors. We believe that H.R. 2944 makes significant progress toward achieving some of these goals, while falling short on others.

We commend the Chairman for the inclusion of provisions on issues that only the federal government can address, including PUHCA repeal and PURPA reform; facilitating state restructuring initiatives by resolving federal/state jurisdictional issues; and addressing a number of transmission and reliability issues, including establishment of a self-regulating reliability organization and extension of FERC transmission jurisdiction over all transmitting utilities. And, we commend the Chairman for not making H.R. 2944 a vehicle for micromanaging competition with punitive market restrictions.

However, we do have concerns with H.R. 2944 in a number of key areas. It fails to develop the same set of rules for all competitors by continuing—and in some cases expanding—federal subsidies to government-owned electric utilities, electric cooperatives and federal electric utilities, and allowing the use of these subsidies in competitive markets. It expands federal regulation by establishing a deadline for regional transmission organizations and increasing FERC's merger authority. The bill also would intrude into state jurisdiction over retail electric service and raise implementation concerns in some areas, including interconnection standards, net metering, aggregation and establishing new FTC standards. We look forward to working with the Chairman and other Members of the Subcommittee to improve these areas of the bill.

We would like to share with the Subcommittee our views on the specific provisions contained in H.R. 2944.

TITLE I—OPEN TRANSMISSION ACCESS

Federal/State Jurisdiction

Section 101 of H.R. 2944 would clarify state authority to order retail competition and to impose nonbypassable charges for public purpose programs. This section also would clarify federal/state jurisdiction over components of an electricity sale, as well as distribution and transmission facilities. We believe that federal legislation needs to address these jurisdictional issues to help reduce uncertainty in electricity markets, and we support their inclusion in H.R. 2944.

Open Access Transmission

Section 102 of the bill would clarify the authority of the Federal Energy Regulatory Commission (FERC) to require all transmitting utilities to provide open access transmission service and to authorize recovery of transition costs arising from any requirement to provide open access transmission. Regarding transition costs, we believe the legislation can be enhanced by the clarification of congressional intent regarding the recovery of transition costs under FERC Order 888. There is a need for certainty in this area—certainty that can be provided only by legislative direction.

EEI strongly supports requiring all transmission providers to be subject to FERC transmission jurisdiction to facilitate efficient use of our nation's transmission system, and we commend the Chairman for including this provision. It does not make sense, from a regulatory standpoint or from a competitive standpoint, to have a significant portion of the transmission system operating under a different set of rules, or in some cases, no rules at all.

However, Section 102 does not extend FERC transmission jurisdiction over the federal electric utilities, including the Tennessee Valley Authority (TVA), the Bonneville Power Administration (BPA) and the other federal Power Marketing Adminis-

trations (PMAs). While this authority is addressed in Title VI of the bill, we recommend that Section 102 be modified to include the federal electric utilities so that all transmitting utilities are covered in this particular section. Title VI is likely to be referred to other committees with jurisdiction over the PMAs and TVA, and those committees may make significant changes to the title.

Section 102 also would allow certain transmitting utilities to exempt themselves from FERC transmission jurisdiction if they meet certain criteria. We are concerned that the self-certification process for exemption could be abused. FERC already has the authority to grant waivers from its transmission regulations to small transmission providers and has granted such waivers in the past. We would reiterate that all transmission needs to be subject to uniform regulation.

Regional Transmission Organizations

Section 103 of H.R. 2944 would require each transmitting utility to establish or join a regional transmission organization (RTO), effective January 1, 2003. EEI supports a flexible, market-based approach to grid regionalization that applies to all transmission providers. We oppose the federal deadline by when utilities must join an RTO.

As any stakeholder involved in the development of the six independent system operators (ISOs) already approved by FERC can attest, the establishment of RTOs is an arduous, time-consuming process that requires a satisfactory resolution of many contentious, critical issues among many interests. Several of the approved ISOs were developed from existing tight power pools; other RTOs will not have this advantage and will be more difficult and take longer to construct. Imposing an artificial deadline on the creation of RTOs will reduce flexibility in evolving transmission markets.

In addition, this federal mandate appears to ignore the tremendous progress already being made at FERC with regard to its notice of proposed rulemaking on RTOs. FERC's proposed RTO rule will further facilitate the voluntary development of RTOs.

Section 103 also would require FERC to approve an RTO application if FERC determines that the RTO meets specific standards outlined in the bill. We agree with the Chairman that if an RTO meets specific standards, including the ones outlined in the bill, FERC should approve the RTO. We recommend that the standards be expanded to include FERC consideration of cost and cost recovery.

However, we are extremely concerned about the provision that would allow FERC to impose any other additional standards it wants on an RTO. We believe Congress should establish RTO standards so prospective RTO participants understand the requirements the RTO must meet in order to obtain FERC approval. Otherwise, prospective RTO participants will be trying to establish an RTO under a cloud of uncertainty that FERC can second guess their decisions by repeatedly modifying RTO standards.

Section 103 would direct FERC to encourage incentive transmission pricing policies for RTOs. This language is essentially the same as the incentive pricing provision in H.R. 2876, introduced by Representative Sawyer. We propose that this provision be modified to extend these incentives to all transmitting utilities, as H.R. 2876 provides, not just those in RTOs. We also support the additional transmission proposals in H.R. 2876. We strongly support reform of FERC's transmission pricing policy, and we appreciate congressional encouragement of reforms.

FERC's current transmission pricing policy does not provide sufficient incentives for construction of critically needed new transmission facilities throughout the country. FERC must reform its transmission pricing policy to facilitate transmission construction in order to assure the continued expansion of competitive markets. In the long run, reliability will suffer, and consumers will be harmed, if new transmission capacity is not built.

Expansion of Interstate Transmission Facilities

Section 105 of H.R. 2944 is intended to help expand interstate transmission facilities. Unfortunately, while we agree with the intent, we are concerned that the section does not achieve its objective. Under this section, a transmitting utility may apply to FERC for an order to expand its transmission. If the utility is unable to obtain the necessary state permits to build the transmission line, the utility may ask FERC to rescind its order.

The chief problem with this section is that the FERC order has no teeth and does not resolve the growing difficulty of obtaining necessary siting permits from a state that may realize little benefit from a transmission line being built to serve interstate commerce. Section 105 requires FERC to consult with a joint federal/state board before issuing an order to build, but the joint board does not have any siting

authority either. Without these teeth, there is no incentive for a utility to seek a FERC order.

We believe that addressing the substantial barriers to expanding the interstate transmission system is probably the most critical transmission policy issue. Without new transmission construction, electricity suppliers and regulators will find themselves fighting increasingly pitched battles over who gets priority for use of an increasingly scarce resource.

TITLE II—ELECTRIC RELIABILITY

EEI participated in the stakeholder process to develop the consensus reliability legislation sponsored by the North American Electric Reliability Council (NERC). Like the other stakeholders, we believe that new, enforceable reliability standards need to be adopted to help ensure our interstate transmission system continues to operate safely and reliably in competitive markets.

We support the inclusion of the NERC consensus language in H.R. 2944, and we appreciate the Chairman's support for this proposal. We would like to comment on the bill's most important modification to the NERC proposal. H.R. 2944 adds a savings clause preserving state authority to ensure the reliability of local distribution facilities. While the states have legitimate reliability concerns, it is important that the self-regulating reliability organization have clear responsibility for assuring the reliability of the interstate bulk power system. Otherwise, the end result may be to weaken overall reliability due to confusion and conflict over who has authority over what reliability responsibilities. EEI, along with other stakeholders, is continuing to work with state entities to develop compromise language to address the states' concerns.

TITLE III—CONSUMER PROTECTION

Sections 301, 302 and 303 would require the Federal Trade Commission (FTC) to promulgate rules addressing electric supplier information disclosure, consumer privacy and unfair trade practices (slamming and cramming). We support measures to protect consumers as they take advantage of choices in a competitive electricity market. Our primary concern with these sections is their potential to preempt existing state restructuring plans. These sections are among the provisions in the bill that tread into state jurisdictional matters relating to retail electric service.

TITLE IV—MERGERS

Section 401 of H.R. 2944 addresses FERC merger authority, while leaving intact merger review by the Department of Justice and the states. On the one hand, the section attempts to expedite FERC's merger review by establishing a timetable for FERC action and substituting the hearing requirement with a procedure for oral and written presentation of views. This appears closer to the approach taken by the Department of Justice. We strongly agree that regulatory review of utility mergers must be expedited, streamlined and simplified. It makes no sense that the BP-Amoco merger—creating one of the world's largest oil and gas companies—could be approved on two continents in less than 100 business days while utility mergers can drag on for two years without resolution. We appreciate that BP Amoco operates in a competitive market, but monopoly utility functions will still remain regulated at both the federal and state levels after a merger to ensure access to essential facilities and to protect consumers.

On the other hand, Section 401 would substantially expand FERC authority by authorizing FERC review of any disposition of generation facilities and holding company mergers, which are not currently within FERC jurisdiction. We are concerned that this language moves in the wrong direction by expanding regulation. A growing number of utilities are selling their generation facilities in order to focus on other business opportunities or to satisfy state restructuring plans. These dispositions of assets are subject to state review. There is no need for additional FERC review under Section 401, which would potentially slow down the move to competition in some states.

Section 401 also would expand FERC authority by requiring FERC to examine a merger's impact on competition in retail markets, another area already subject to state review. FERC examines a merger's effect on wholesale competition, but requiring FERC to examine the impact on retail markets clearly intrudes on the states' jurisdiction and unnecessarily duplicates existing regulation.

We understand that some entities argue for even more burdensome utility merger review. They want electric utilities to be subject to higher merger standards than any other industry, even though utility mergers already are subject to more regulation than literally any other industry. Proponents of these draconian proposals claim

that utility mergers will dramatically reduce the number of competitors. We would point out that there are thousands of suppliers who currently participate in electricity markets, with many new entrants—among them the world's largest oil and gas companies—getting into the market. Claims that the electricity market will somehow lack competitors are both ludicrous and blatantly inaccurate.

TITLE V—PROMOTING COMPETITION

Retail Reciprocity

Section 501 would impose a mandatory reciprocity provision on the states. We believe the section should be modified to clarify state authority to impose reciprocity requirements on suppliers if a state chooses to do so. Otherwise, this section as currently written would preempt existing state restructuring plans in a number of states, including California, which consciously chose not to impose reciprocity requirements on suppliers in their state restructuring plans. We would prefer a provision which facilitates, rather than intrudes, into state decisions relating to reciprocity.

Public Utility Holding Company Act (PUHCA)

Subtitle B of Title V would repeal PUHCA 12 months after enactment and substitute a new act giving FERC and state regulatory commissions access to the books and records of holding companies and affiliates. PUHCA is an impediment to competitive markets that only Congress can address, and we strongly support inclusion of this subtitle in H.R. 2944. PUHCA was enacted in 1935 during the New Deal in response to conditions in the electricity industry at that time. However, like everything else, the electricity industry has obviously changed over the past 60 years, and it is time that PUHCA be changed to recognize this fact.

Public Utility Regulatory Policies Act (PURPA)

Subtitle C of Title V would reform PURPA by repealing prospectively the mandatory purchase obligation, protecting existing contracts and providing for the recovery of federally mandated, FERC jurisdictional PURPA costs. We strongly support inclusion of these provisions in H.R. 2944, including those addressing PURPA cost recovery. A federal statute that forces utilities to purchase power at above-market prices, regardless of whether they need that power—and consequently forces consumers to pay billions of dollars more for power than they otherwise would—cannot be justified in a competitive market.

Aggregation

Section 541 of the bill would preempt all other federal and state laws addressing aggregation, except those relating to undue discrimination and preferential treatment, to allow any entity, including an electric cooperative or municipality, to aggregate retail consumers in open states.

EEI believes that consumers who have retail electric choice should be able to choose any qualified supplier they wish, including one that aggregates them with other customers. However, we oppose any government-initiated slamming that would force all customers in a particular area or group to switch suppliers, even if they later have the opportunity to opt out of such a forced switch. We are concerned that the preemptive provisions of Section 541 would allow a municipality, cooperative or other entity to force an entire group of customers to switch suppliers.

In addition, we are concerned that the provisions in Section 541 that preempt state law are so broad that they could undo other important public policies. For example, these provisions appear to allow an electric cooperative or municipality that is required by state law to operate only within its own discrete service territory to jump the fence and compete outside that service territory.

We would be pleased to work with the Chairman to modify the language of this provision to assure that any service provider in open states may aggregate consumers who voluntarily choose to purchase electricity from that provider, consistent with applicable rules for obtaining electric service.

Interconnection

Section 542 would give FERC the authority to order interconnections to utility distribution systems for distributed generation facilities. Distributed generation obviously will play an increasingly important role in meeting consumers' power needs in a competitive market. EEI, along with other groups, is working with the Institute of Electrical and Electronics Engineers (IEEE) to develop a uniform interconnection standard regarding reliability and safety issues relating to distributed generation facilities. IEEE is the organization that has the technical, engineering, reliability and

safety expertise to assure the standard results in the safe integration of distributed generation into the distribution system.

We have several concerns with Section 542. First, the bill defines a distributed generation facility as a facility of 50 *megawatt* capacity or less that is designed to serve retail electric consumers at the facility. Fifty megawatts is a lot of power; a facility this size is not one that average consumers would install in their homes or small businesses to meet their basic power needs. Fifty megawatts would be large enough to meet the peak electricity demand of a small city of roughly 6,000 homes. Utilities do not connect 50-megawatt generation facilities to their distribution systems; instead, these would have to be connected to bulk-power transmission systems. Forcing a utility to connect 50-megawatt generation facilities to its distribution system would create serious reliability and safety problems.

Second, Section 542 would give FERC authority to order utilities to increase their distribution capacity in order to carry out a FERC interconnection order. This is a clear intrusion of federal authority into the states' traditional regulation of distribution service. At the same time, Section 542 does not address the crucial issue of who pays for any required upgrade in distribution capacity. While FERC would be able to order distribution upgrades, the authority for allowing the recovery of the cost of such upgrades would remain with state commissions, with no assurance of any cost recovery. We believe authority to order distribution upgrades should remain with the states, which regulate distribution activities.

TITLE VI—FEDERAL ELECTRIC UTILITIES

Electricity restructuring cannot achieve its anticipated results unless the rules governing competition treat all competitors alike. This proverbial "level playing field" among different *types* of electricity providers requires similar tax and regulatory treatment, similar access to investment capital and similar access to preference right power on behalf of our respective consumers. If the current subsidies available to public and cooperative power are available to be used to construct new generation or transmission facilities in a restructured electricity marketplace, then we will have multiple sets of competitors operating under multiple different sets of rules. Shareholder-owned utilities would be at considerable disadvantage in such an environment, not because other competitors are more efficient or better managed, but because they have better access to government subsidies. Unfortunately, Title VI does not address these issues; in fact, the title would make matters significantly worse.

Subtitle A—Tennessee Valley Authority

Section 602 repeals certain provisions of the Federal Power Act dealing with interconnections, wheeling and portions of the TVA Act establishing the "fence" around TVA's service area. Section 603 limits TVA's sales to retail customers, authorizes the sale of "excess" TVA power and electricity exchanges outside its service area and applies various Federal Power Act requirements to TVA.

TVA is a heavily subsidized government utility. Permitting TVA to sell its subsidized power beyond its service area raises the specter of unfair competition and undermines this bill's purpose of promoting real competition in electricity markets. The section provides no meaningful guidance on how TVA power is to be sold.

Section 604 provides that TVA may issue bonds for new or enhanced generating facilities if TVA determines they are necessary to supply the demands of distributors and retail consumers. In tandem with Sections 602 and 603, this means that TVA can sell its subsidized power over the fence and then issue bonds to build capacity to meet its internal needs. TVA has plenty of generating capacity, as evidenced by its easily meeting power needs on sixteen record degree days during this summer's extraordinary heat wave and drought. The only reason for Section 604 is to permit TVA to acquire new generating capacity for anticipated sales beyond its service area. We believe there is no reason for TVA to build new capacity in a competitive generation market.

TVA operates under a $30 billion debt ceiling established by Congress and currently has outstanding obligations of roughly $26 billion. These bonds are not guaranteed by the full faith and credit of the United States government, but they are perceived as such by bond rating agencies and investors. The federal government has never allowed a wholly owned federal corporation to go bankrupt and those who sell and own bonds are banking on an "implied guarantee" that does not exist. Nonetheless, this association with the financial strength of the federal government gives TVA bonds an AAA rating and enables TVA to borrow at rates substantially below those of similarly situated utilities.

A ten-year plan TVA issued two years ago articulated a goal of reducing TVA's debt by half over the ensuing decade. TVA has made little progress towards this

goal and, in fact, has already slipped two years in its timetable. Allowing TVA to slip even further into debt courts fiscal disaster. We believe Congress should take TVA at its word and lower its debt ceiling along the schedule outlined in its ten-year plan.

Section 605 permits TVA to renegotiate its long-term contracts with distributors. This is fair to the distributors who must now give ten years notice before they can leave TVA's system or buy power from other vendors. These contracts effectively preclude the entry of new competitors in the Tennessee Valley. It will take some time for TVA to renegotiate these complicated agreements with 159 distributors and even longer to agree on the treatment of stranded costs, as outlined in Section 608. At a minimum, TVA's over-the-fence sales should not begin before these agreements are reached and outside competitors have the same access to Tennessee Valley customers that TVA has to customers on the other side of the fence.

Section 609 applies federal antitrust law to TVA but not the sanctions that make such laws effective. We believe TVA should be covered in the same manner as other utilities.

Section 612 says that Subtitle A "shall be interpreted and implemented in a manner that does not adversely affect bonds issued by the Tennessee Valley Authority." We cannot imagine a larger loophole. It puts the interests of TVA's bondholders ahead of those of America's taxpayers, the true owners of TVA. This section should be removed.

Without changes, Subtitle A would unleash an enormous subsidized electricity vendor into the competitive marketplace this legislation is supposed to create. It does not address TVA's staggering debt and, in fact, encourages TVA to borrow still more. It equips TVA with special exemptions from law and, in its final section, essentially absolves TVA of the most basic regulatory constraints.

Subtitle B—Bonneville Power Administration

Section 623 would authorize Bonneville Power Administration (BPA) to impose a surcharge of up to $100,000,000 per annum on its transmission customers. These revenues would be used to pay off debt Bonneville has incurred in acquiring generation capacity. The surcharge could ostensibly only be imposed if Bonneville projects "that available financial reserves in the Bonneville Power Administration Fund attributable to the power function will fall below $150,000,000." The section also provides for FERC oversight.

We strongly oppose this surcharge. Since federal transmission regulation began in the 1930s, policy has been that those who use power pay for its generation and those who use transmission capacity pay only for transmission. Under Section 623, in many cases, transmission customers would be forced to pay for electricity that someone else actually uses. There also would be situations where the transmission customer paying the surcharge would be paying for generating capacity acquired to compete against its own. In truth, BPA's current customers—more than two thirds of whom are industrial facilities—can easily afford to cover BPA's generating costs: It would require a rate increase of less than two tenths of a cent per kilowatt hour.

Section 625 authorizes "acquisition of new major generating resources." We believe this is a good example of "mission creep." BPA was established to sell the power produced at 29 federal hydroelectric facilities on the Columbia River system. It has gradually metamorphosed into a utility with a much larger role in the Pacific Northwest. We believe BPA should return to its mission and concentrate on marketing and distributing the power from federal dams. There is no rationale for BPA to acquire or construct new thermal generating capacity in a competitive environment when other suppliers are willing to do so.

Like the similar provision in the TVA subtitle, Section 626 applies federal antitrust law to BPA but without the economic penalties other entities face. If BPA wants to be a player in competitive markets, it should face the same laws and penalties that other players face.

Section 627 calls for "encouraging the widest possible diversified use of electric power *at the lowest possible rates* to consumers consistent with sound business principles." (emphasis added). We believe the foundation principle of BPA should be what it is for virtually every other federal agency responsible for the management and sale of the public's resources: To achieve for America's taxpayers the best possible price or "fair market value" whenever public assets are sold.

The federal government routinely sells coal, oil, natural gas, timber and other assets. The prime responsibility of agencies like the Minerals Management Service, the Bureau of Land Management and the Forest Service is to ensure receipt of "fair market value" when the public's assets are sold. There are open and public bidding procedures under which the high bidder wins. There is administrative and judicial

review and close congressional oversight. These programs bring to the Treasury billions of dollars per year in revenue.

No such regimen covers BPA's sale of electricity produced at federal generating facilities. We are referring here not to the preference right power sold within BPA's traditional service area but to the power BPA sells outside the Pacific Northwest or "over the fence." This power is sold through nonpublic negotiations and the prices are not released. No other federal assets can be sold in this way. Imagine the umbrage in Congress if the Department of the Interior sold coal or oil tracts through a secret process and at a secret price.

We propose a system for the "over the fence" sale of Bonneville power, one modeled after the successful systems for selling other federal assets. Nothing less will ensure taxpayers that government is receiving top dollar on the sale of their assets.

TITLE VII—ENVIRONMENTAL PROVISIONS

We commend the Chairman for not including a mandatory renewable energy portfolio standard in H.R. 2944. A renewable portfolio standard is a hidden tax on all consumers that would force them to pay more for electricity. Polls demonstrate that many consumers will voluntarily pay more to purchase electricity from renewable energy sources, and consumers in open states should have this option. We believe the Chairman has included more appropriate incentives to promote renewable energy, including the renewable energy production incentive and the renewable energy tax credit.

Net Metering

Section 702 of H.R. 2944 addresses net metering service. Again, net metering relates to the provision of retail electric service; these issues are being addressed by the states, and Section 702 is an intrusion in state jurisdiction. Further, net metering should apply only to the energy portion of the bill and not relieve a consumer from paying other charges on the bill, including those for public policy purposes and distribution services.

TITLE VIII—PROVISIONS RELATING TO INTERNAL REVENUE CODE

For competition to work, Congress needs to address the artificial competitive advantages provided by the tax exemptions and tax-exempt financing used by government-owned utilities and electric cooperatives when competing against other electricity suppliers, so that all competitors can participate in open markets under the same set of rules. For this reason, EEI has concerns with section 801 and 802 of the bill.

Business Activities of Mutual or Cooperative Electric Companies

Section 801 would remove the requirement that electric cooperatives and similar organizations pay taxes on income from sales to nonmembers to the extent that income exceeds 15% of revenues. Federal subsidies have been given to electric cooperatives on the argument that they are nonprofit organizations serving only their owner-members.

We believe that section 801 goes too far when it allows electric cooperatives to retain their tax-exempt status while making an unlimited amount of sales to nonmembers. Also, we do not feel it is warranted to permit electric cooperatives to exclude debt written-off as an exclusion from the 85% member income test.

Tax-Exempt Bond Financing of Certain Electric Facilities

EEI has major concerns with section 802 because it provides expansive relief to government-owned utilities, even if they do not fully open to competition, and allows them to issue new tax-exempt bonds for new transmission and generation facilities that will compete with privately owned, taxpaying entities. These provisions also would provide substantial loopholes allowing government-owned utilities to sell electricity for profit outside their service territories without paying income taxes on these sales. The provisions would distort competitive electricity markets by helping government-owned, subsidized utilities to expand at the expense of tax-paying electricity suppliers.

In contrast, the Administration has proposed a much different approach to dealing with the tax consequences of electricity restructuring. Their proposal would grandfather outstanding bonds for government-owned utilities that offer choice to their consumers, but would eliminate the ability to issue any tax-exempt debt *in the future* for all facilities involved with transmission or generation of electricity. Legislation (H.R. 1253) introduced by Representative English takes a similar approach as the Administration, but would take the additional step to tax profits on sales made outside of a government-owned utility=s service territory. EEI believes either of

these approaches is more equitable than H.R. 2944 as they provide for competition to take place on a more level playing field. Consumers deserve to receive true market signals as they choose their electric supplier. Subsidized power does not give them the true signals of efficiencies and lowest costs.

Nuclear Decommissioning Costs

EEI strongly supports section 803 of the bill, the provisions of which were introduced by Representative Jerry Weller (H.R. 2038). The need for this section results from the evolution from a regulated environment to a competitive electricity market. Because of this structural change, the tax treatment of nuclear decommissioning funds is not clear under current law. In addition, restructuring has brought regulatory and market forces to bear upon continued ownership of nuclear power plants, resulting in transfers and sales of these plants. In some instances, state restructuring laws *require* divestiture of power plants. These activities have triggered unforeseen tax consequences that, if not corrected, could force the early shutdown of nuclear units that cannot be sold, resulting in the loss of jobs and a reduction of energy supply.

The provisions in this section will address needed reforms to U.S. tax law associated with decommissioning of nuclear power plants in a deregulated market by: (1) eliminating the cost of service requirement; (2) defining nuclear decommissioning costs and clarifying that all such costs are currently deductible; (3) allowing for the transfer of nonqualified funds to a qualified decommissioning fund; and (4) providing for the tax-free transfer of these funds when nuclear assets are sold to a nonregulated entity.

Renewable Energy Tax Credit

EEI supports section 804, which would extend the tax credits for electricity generated by wind and biomass.

OTHER ISSUES

In addition to commenting on what is in H.R. 2944, we want to commend the Chairman for what is *not* in the bill. Of utmost importance, we are pleased that the bill does not grant FERC new authority to order utilities to divest their assets nor does it impose competitive handicaps on the ability of utilities and their affiliates to offer new services and products.

Federal legislation should protect competition, not competitors; it should not become a vehicle for favoring new entrants by breaking up or otherwise handicapping the ability of existing utilities to compete. Recent polls conducted by EEI show that 91 percent of American consumers believe that their current electricity supplier should remain in the mix of competitors from which they can choose.

Any evaluation of market power issues must look to where the electricity industry is rapidly heading, not to where it has been, or even where it is right now. Proponents of draconian market power proposals act as though monopolistic utilities are about to be completely deregulated to run amok in a competitive market.

To the contrary, in competitive electricity markets, utility monopoly functions will continue to remain regulated at both the federal and state levels to ensure all competitors access to essential facilities and to ensure that distribution utilities do not cross subsidize or provide unfair preferences to their affiliates. A number of different federal and state statutes address potential market power problems. In addition, state restructuring plans are addressing potential market power concerns.

And, let's not ignore what is already occurring in evolving competitive electricity markets: thousands of competitors currently exist, with many more large, established companies with significant name recognition entering the market. Tens of thousands of megawatts of new generation is being planned, which will be constructed and brought on line much more quickly than in the past. In addition, utilities are selling tens of thousands of megawatts of their own generation.

Market share simply does not equal market power. As long as consumers have a choice of suppliers, a company can serve a large portion of the market without having the ability to manipulate prices or prevent other suppliers from competing. In competitive markets, sellers offer different advantages to consumers, and they cannot be equalized. The ability to bring lower prices or better services to consumers is what competitive markets are all about.

CONCLUSION

We support legislation that removes federal barriers to competition, facilitates state restructuring activities, addresses critical transmission and reliability issues and applies the same rules to all competitors. We believe that H.R. 2944 makes significant progress toward achieving some of those goals, while falling short on others.

We commend the Chairman for his continuing efforts to develop a workable electricity bill, and we look forward to continuing to work with him and other Members of Congress to address our concerns with H.R. 2944.

Mr. BARTON. Thank you, Mr. Owens.

We would now like to hear from Ms. Lynne Church, who is executive director of the Electric Power Supply Association and, just as a personal aside, is an expert on traffic congestion in northern Virginia.

Ms. CHURCH. Mr. Chairman, you are stealing my speech.

Mr. BARTON. Welcome. Your statement is in the record and we give you 6 minutes to summarize it.

STATEMENT OF LYNNE H. CHURCH

Ms. CHURCH. Thank you.

Good morning, Mr. Chairman, Mr. Hall, and members of the committee.

My name is Lynne Church. I am the executive director of the Electric Power Supply Association, which is the national trade association for the competitive power supply industry, including power marketers and non-regulated generators active in the United States, as well as U.S. global markets.

I thank all of your for the opportunity to present my testimony and our analysis of H.R. 2944.

The bill focuses primarily on the wholesale marketplace. While EPSA's vision of the future certainly demands a national competitive market for electricity, there is a very broad consensus that additional Federal legislation is needed to promote truly competitive wholesale power markets.

We do not yet have full comparability of rates, terms, and conditions for interstate transmission service. Barriers to entry for new market participants remain. It may surprise the subcommittee, but many of EPSA's members actually believe the wholesale market is getting less, not more, competitive.

The long-term success of your effort will be linked to a simple question: does this law make wholesale power markets more robust, more fair, and more competitive? This question has real-world implications for your constituents and consumers, in general.

Just last week, for example, the local electric utility, PEPCO, announced a 7 percent rate reduction. Fully half of this reduction is attributed to cost savings associated with increased reliance on the wholesale markets.

H.R. 2944 is complex, and EPSA clearly agrees with many of the provisions; however, one area of significant concern relates to the regulatory oversight of the interstate transmission grid. If this legislation is to be pro-competitive, it must make absolutely clear that all users of the interstate system are subject to a consistent set of rules overseen by a national regulatory body.

Unfortunately, in three separate provisions, the bill unnecessarily subjects the interstate grid to potentially intrusive State control. Any one change would be problematic, but the combination of the three has the potential to defeat the creation of a truly competitive and efficient marketplace.

The bill clarifies that Federal authority is limited to unbundled power sales, or those sales where customers are billed separately for power generation and transmission services.

For those 24 States—we count 24—which have adopted a framework of retail competition, all power sales are essentially becoming unbundled. In those States, Federal authority will extend to all uses of the interstate grid. However, as long as some States opt against retail choice, this legislation will perpetuate a system where large portions of the interstate grid will remain outside of Federal control and subject to State control. And those States that have moved to competition may well be penalized in terms of serving their customers.

It is akin to suddenly turning an eight-lane superhighway into a bumpy country road once it reaches a political boundary of a State.

This jurisdictional split will create risk in the marketplace and may lead some States to engage in ill-conceived attempts to protect in-State consumers at the expense of out-of-State power users.

To use the highway analogy again, imagine what would happen if northern Virginia decided to mitigate road congestion during rush hour by permitting only cars with Virginia tags on its highways and excluding DC and Maryland drivers from its roads during those hours.

The subcommittee needs to recognize that our grid is truly interstate from an engineering standpoint, and even small disruptions can have broad impact.

For example, we believe that a poorly managed effort to curtail 400 megawatts of power flowing between Ontario and Michigan this past July led ultimately to the dramatic price spike in Illinois, Indiana, and Ohio that we have read about, and to hundreds of millions of dollars in unnecessary costs.

This distinction between unbundled and bundled uses of the transmission grid is an artificial and unnecessary one. It is fundamentally at odds with the concept of full comparability and an effort to promote a robust competitive power place.

The other two areas of which I speak are the areas dealing with grid reliability and the determination of transmission versus distribution assets.

The bill in those areas further interjects State regulators in issues that are best considered at a national level.

In a number of other areas, the legislation has been significantly improved since the initial draft in August, and we appreciate the Chair and the committee's and the staff's role in listening to us and including some of these provisions.

Particularly, the bill's language on mergers, regional transmission organizations, and new plant interconnections are very positive steps. They do not resolve all our concerns, but they are definitely a step in the right direction. And I refer you to the text of my written comments for some suggested refinements to those provisions, as well as to the PURPA and renewable power section.

Some subcommittee members have expressed opposition to any new authority to FERC, yet, we do not believe that FERC needs a greatly expanded role. Instead, the Commission's existing authority needs to be clarified and FERC's role encouraged to evolve.

Competitive power markets will continue to rely on an interstate grid that is a monopoly provided service. As such, these markets will require the presence of an effective watchdog, and FERC is, realistically, the only agency equipped to handle this responsibility.

To summarize, enormous consumer benefits can be achieved through the enactment of pro-competitive wholesale power legislation, but the system today is broken. Without action by this Congress, your constituents and consumers, generally, will be threatened with unnecessary market volatility and higher prices for power.

[The prepared statement of Lynn H. Church follows:]

PREPARED STATEMENT OF LYNNE H. CHURCH, EXECUTIVE DIRECTOR, ELECTRIC POWER SUPPLY ASSOCIATION

Mr. Chairman, Ranking Minority Member, and Subcommittee Members, my name is Lynne H. Church, Executive Director of the Electric Power Supply Association (EPSA). EPSA is the national trade association that represents the leading competitive power suppliers—including power marketers and developers of competitive power projects—active in the U.S. and global energy markets. On behalf of the competitive power industry, I thank you for this opportunity to present our analysis of your legislation to restructure the electric power industry, H.R. 2944, the Electricity Competition and Reliability Act.

The Goal of Legislation: Building a Robust, Competitive Wholesale Power Market

As you know, H.R. 2944 focuses primarily on the wholesale marketplace. While EPSA's vision of the future demands a national, competitive retail market for electricity, our experience in today's wholesale markets underscores the potential value of your legislative efforts.

As testimony before the Subcommittee has made clear, there is a broad consensus that much still needs to be done. True comparability of rates, terms and conditions for interstate transmission service for all classes of customers has yet to be achieved. Barriers to entry for new market participants remain. The monopoly providers of transmission services are learning to use their systems in ways that can be at odds with a competitive marketplace. It may surprise the Subcommittee that many of EPSA's members actually believe the wholesale market is getting *less*, not more competitive.

The long-term success of your effort will be linked to a simple question: does this law make wholesale power markets more robust, more fair and more competitive? While issues in the wholesale market directly concern electric power distribution companies, power producers and marketers, this question has real world implications for your constituents. Just last week, for example, the local electric utility PEPCO announced a seven percent rate reduction. Fully half of this reduction is attributed to cost savings associated with increased reliance on wholesale markets. We believe the impacts on consumers are direct: more competition, more benefits; less competition, less benefits and higher costs.

H.R. 2944 Splits Jurisdiction Over the Interstate Market and Could Increase Risk

H.R. 2944 represents a complex policy proposal and we recognize that the legislative process will result in a stream of changes and new ideas. We look forward to working with the Subcommittee as this process unfolds and are optimistic that our collective efforts can result in critically needed, pro-competitive legislation.

While EPSA clearly agrees with many provisions in the legislation, there are issues that need further action or alternative solutions. As one area of significant concern, we raise the issue of regulatory jurisdiction over the operation of the interstate transmission grid. If this legislation is to be pro-competitive, it must make absolutely clear that all users of the interstate system are subject to a consistent set of rules overseen by a national regulatory body. Unfortunately, in three separate provisions, the bill unnecessarily subjects the interstate grid to potentially conflicting and disruptive regulatory control. Any one change would be problematic, but the combination has the potential to defeat the creation of a truly competitive and efficient marketplace.

First, the bill clarifies that federal authority is limited to "unbundled" power sales. An unbundled sale is one where a customer is billed separately for power generation and transmission services. "Bundled" sales are where a customer gets a single bill for electric service and typically has no choice of power provider.

As states move to retail competition, all power sales essentially become unbundled: this is critical to the concept of customer choice. Hence, in a world where all the states have embraced retail competition (as 24 have done already), federal authority extends to all uses of the interstate grid. On the other hand, as long as states opt against retail choice, your legislation perpetuates a system where some uses of the interstate grid are subject to state control, while others are in a national system.

In many states, "bundled" uses of the interstate grid amount to 80% or more of the transactions on the interstate grid. As written, this legislation has the possible effect of reducing the interstate grid—our interstate highway system for power—from an eight lane super highway to a dirt road. In addition, this jurisdictional split may permit some states to engage in ill-conceived attempts to protect instate consumers at the expense of out-of-state power users. Continuing with the highway metaphor, imagine what would happen if Northern Virginia decided to mitigate road congestion by permitting only cars with Virginia license plates on its highways during rush hour?

The Subcommittee needs to understand that, regardless of legal jurisdiction, our grid is truly interstate and even small local disruptions can have broad impacts. For example, we believe that a poorly managed effort to curtail 400 Mw of power from flowing between Ontario and Michigan led ultimately to a dramatic price spike in Illinois, Indiana and Ohio last summer and to hundreds of millions of dollars in unnecessary costs for consumers.

The distinction between unbundled and bundled uses of the transmission grid is an artificial and unnecessary one. Separate treatment and regulatory oversight makes impossible a system of consistent rules and comparability with respect to transactional rates, terms and conditions. Such a split in jurisdiction creates potentially overwhelming commercial risk. It also is fundamentally at odds with any effort to promote a robust competitive wholesale power marketplace.

In two other areas, as part of the sections dealing with grid reliability and the determination of transmission assets, the legislation interjects state regulators in issues that are best considered at a national level. Rules governing grid reliability, for example, have regional, national and commercial impacts. Allowing fifty states broad rights to "adjust" these rules to reflect local concerns is a formula for potential chaos in the wholesale marketplace.

In addition, there is growing concern in the marketplace that, through a process known as "refunctionalization," the owners of transmission assets will attempt to reclassify these transmission facilities as elements of the distribution network. In part, such actions will be taken to avoid federal oversight. This effort, it is feared, will effectively shrink the physical marketplace and result in potentially increased congestion and supply disruptions. If transmission owners are allowed to appeal to local interests and authorities for these determinations, a consistent set of rules will be impossible and erosion of the interstate transmission system could result. While the perspective and advice of local authorities can be invaluable, the legislation must make clear that local concerns cannot trump the national interest.

H.R. 2944 Includes Improved Market Power Provisions, But More Work Needed

In a number of other areas, the legislation has significantly improved since the initial draft was released in early August. Three such provisions relate to the bill's language on mergers, regional transmission organizations (RTOs) and new plant interconnection with the interstate grid. While not resolving our concerns with respect to the abuse of market power in the marketplace, these provisions represent a step in the right direction.

Even in these areas, however, we encourage you to adopt further refinements. For example, independent control is absolutely essential to the operation of a commercially acceptable RTO. However, the legislation defines any RTO where participants each own less than ten percent of voting stock as "independent." This language should be changed—an RTO where six transmission owners control 60% of the voting rights meets few market participants definition of "independent." As another example, we note that the bill's provisions to ensure that the non-discriminatory interconnection of new power plants improve on the status quo. Nevertheless, the process outlined in the legislation is still insufficiently streamlined to have a significant, positive impact.

Lastly, we urge the Subcommittee to ensure the capability of federal regulators to react in near "real-time" and with direct, but light-handed, remedies to allegations of market power abuse. EPSA members do not see the courts or anti-trust laws as a viable approach to resolving market power issues on a day-to-day basis. The markets and participants are changing rapidly. Litigation, especially when antitrust laws are involved, is unwieldy, extremely expensive and unlikely to lead to a

rapid resolution of concerns. Given these circumstances, justice delayed will mean justice denied for many market participants.

While some Subcommittee members have expressed opposition to any new authority at FERC, we do not believe that FERC needs a greatly expanded role. Instead, the Commission's existing authority needs to be clarified and FERC's role encouraged to evolve. Competitive power markets will continue to rely on an interstate grid that is a monopoly-provided service. As such, these markets will require the presence of a effective watchdog and FERC is realistically the only agency equipped to handle this responsibility. States acting on their own cannot serve this role. On the contrary, acting on their own, states could exacerbate the problems facing the industry.

Additional PURPA and Renewable Power Provisions are in Order

Before closing, we would like to comment on two other sections in the legislation, relating to PURPA and renewable power. For some time, EPSA has supported the prospective repeal of PURPA's mandatory purchase obligations, linked to the introduction of competitive retail markets. If PURPA is amended in federal law, *there must be explicit recognition and preservation of existing PURPA contracts.* We also endorse your efforts to guarantee the recovery of PURPA contract costs as appropriate federal policy. However, such cost recovery must be explicitly related to the *honoring of existing contracts.* Lastly, EPSA urges the *repeal of the ownership restrictions on PURPA Qualifying Facilities (QFs).* In 1992, the Congress placed no such restrictions on Exempt Wholesale Generators (EWGs) and the time has come for similar treatment for QFs.

EPSA also endorses additional support for renewable resources. The bill's Renewable Energy Production Incentive is unfairly focused on non-profit companies. This program should be expanded to cover all types of companies. Alternatively, the tax credit for renewables included in the legislation should be expanded to include the full range of technologies covered by the Incentive program (i.e., "solar energy, wind, biomass, or geothermal").

Conclusion

EPSA's members are very appreciative of this opportunity to share with the Subcommittee our views of your legislation and the state of competition in wholesale markets. We look forward to working with the Subcommittee and the full Committee to ensure the creation of critically needed, pro-competitive legislation.

To summarize, enormous consumer benefits can be achieved through the enactment of pro-competitive wholesale power legislation. We are not advocating intrusive "re-regulation," as some might claim. Rather, we advocate light-handed, consistent oversight of all competitive aspects of the industry with appropriate enforcement policies and national regulation of the monopoly interstate transmission network. Today, the system is broken. Without action by this Congress, your constituents will be threatened with unnecessary market volatility and higher prices for power.

Mr. BARTON. Thank you.

We now want to hear from Mr. William Mayben, who is the president of Nebraska Public Power in Columbus, Nebraska. He represents the Large Public Power Council.

Your statement is in the record. We welcome you. We hope that when Texas A&M plays Nebraska in a month that there is a power outage in the big red machine on the football field, but certainly not in the utility grid.

Mr. Mayben.

STATEMENT OF WILLIAM R. MAYBEN

Mr. MAYBEN. Nebraska has been known to have a power outage in the second half for just a strategic thing.

Thank you, Mr. Chairman.

Nebraska Public Power District is a vertically integrated electric utility that serves about 1 million of the 1.6 million people that live in Nebraska. That does not sound like very much, based upon some of the numbers I have been hearing, but for us it is pretty important.

The Large Public Power Council is represented by 21 of the largest publicly owned State and locally owned electric utilities in the country. We have about 6 million customers in total, about 44,000 megawatts of generation, and about 25,000 miles of high-voltage transmission lines.

Now, we distinguish ourselves from the dominance of the electric utility industry in that we do not engage much in mergers—in fact, none at all—and, for the most part, we are not interconnected with either one of ourselves, so we truly depend upon the national grid.

The Large Public Power Council applauds the chairman's efforts in bringing together a comprehensive bill to deal with deregulation of the electric industry. As it is formed, we believe for the most part, it will be very beneficial for the consumers throughout the United States.

We have two fundamental issues with regard to the bill, as it is drafted, and we are really pleased with the way it is going, but we have a little bit of problems. Our problems are pretty well laid out in the details of my prepared testimony.

The first thing we have problems with is in the private use area. As you know, private use was really imposed upon public power entities issuing tax-exempt debt to construct transmission lines and power plants back in the 1986 Tax Reform Act. That act clearly was passed in contemplation of the regulated monopoly utility industry that we had at that point in time.

As we go forward with deregulation, it is clear that that act does not fit a segment of the electric utility industry very well, and we believe that it has to be addressed.

Fundamental limitations that we face are that we can only issue or we can only take about 10 percent of the output of our generation or our transmission and use it in an open competitive market, or derive only about $15 million a year in the engagement of the wholesale market.

We believe the transmission issue that is most troublesome to us—and, by the way, we support very strongly the work that is necessary to create a robust transmission system throughout the United States. We think that is the key to a competitive market, and we think if we can accomplish a competitive market, many of the other things that we are concerned about with regard to market power will be ameliorated, to some extent.

A fundamental problem is that public power is different than investor-owned utilities. We are required, for the most part, to abide by the statutes and the rules that are set forth in our legislatures and in our home communities, and those rules are contrary to the rules that the investor-owned utilities can abide by with Federal jurisdiction.

We believe that the bill needs to recognize that public power is different, that the rules that we are asking for with regard to jurisdiction by the Federal Government recognizes our situation.

With regard to the creation of RTOs, the public power entities support that, and we believe very strongly that they should be a part of the regional transmission organizations. But, again, we believe that we need to be given the recognition of the uniqueness of public power in terms of becoming members of the RTOs.

We are concerned, at this stage of the game, that, if we do not have that kind of recognition, we will find ourselves without the ability to participate in the RTOs, and we think that the market will be affected by our absence. So we urge you to contemplate that we be given some special consideration.

In conclusion, again we applaud the chairman and the committee for coming forth with a comprehensive bill. We think it is the step in the right direction. We would like to work with you as much as we possibly can to see to it that our particular needs are addressed.

[The prepared statement of William R. Mayben follows:]

PREPARED STATEMENT OF WILLIAM R. MAYBEN, PRESIDENT, NEBRASKA PUBLIC POWER DISTRICT ON BEHALF OF THE LARGE PUBLIC POWER COUNCIL

My name is William Mayben, and I am President of the Nebraska Public Power District. I am testifying today on behalf of the Large Public Power Council. We appreciate the efforts that Chairman Barton and this Committee have made to assemble a comprehensive electric industry restructuring bill that aims to benefit all consumers. Today I would like to comment specifically on several aspects of Chairman Barton's bill that are of paramount importance to our members.

The Large Public Power Council ("LPPC") is an association of 21 of the largest state and locally-owned electric utilities in the United States. Our members serve approximately 6,000,000 retail customers, and own and operate over 44,000 megawatts of generation. In addition, we own and operate in excess of 24,000 circuit miles of transmission lines. LPPC's members are located throughout the country in states including Washington, Texas, Arizona, California, Florida, Georgia, New York and Tennessee.

We have reviewed Chairman Barton's bill, and overall, we believe the bill takes some positive steps towards encouraging a competitive and healthy electricity market. We do support the comprehensive approach to restructuring reflected in the bill, but have some specific concerns regarding several provisions. As I will outline in my testimony, we believe that any comprehensive restructuring bill must both satisfactorily resolve the private use issue and recognize that the federal government must not regulate state and municipal agencies as if they were private corporations. Given these overarching principles, I will focus my comments on several aspects of the bill that are of the greatest interest to our consumers, who will ultimately either bear the brunt of, or enjoy the benefits of, federal legislation. Those issues are private use restrictions, proposed new powers for FERC that would extend to public power transmission, and participation in Regional Transmission Organizations (RTOs).

Private Use

I will begin with the most compelling issue for LPPC's members and consumers today—private use restrictions. Private use restrictions form a serious barrier to open competition and consumer choice. Failure to provide relief from some of these restrictions will preclude many public power systems from opening their systems to full competition and could result in higher rates for consumers. Such a result would be contrary to the goal of providing a competitive market that is open to all who wish to participate, ultimately to the benefit of all consumers. Unless public power systems are provided with private use relief, many of us will not be able to be full participants in a competitive marketplace and thus would have little stake in advancing federal restructuring legislation. We would like to work with this Committee to craft fair, effective and comprehensive restructuring legislation—but it must be comprehensive. We cannot support federal restructuring legislation without effective private use relief.

Background

By way of background, public power systems have no practical source of external financing other than the municipal debt markets. Unlike private companies, public entities cannot issue stock. The private use rules that apply to our financing, most recently revised by Congress in the 1986 Tax Reform Act, were promulgated prior to the advent of a competitive electric industry. The rules provide that no more than the lesser of 10 per cent, or $15 million, of power generated by a power plant financed with tax-exempt debt, or transmission capacity of a transmission line financed with tax-exempt debt, may be sold to a private entity under a customer-specific contract. In simpler terms, the rules preclude us, for most transactions, from

providing open access transmission and distribution services and from offering competitive prices for power sales.

In the regulated monopoly world that existed prior to competition, this restriction was problematic but manageable. In a competitive world of open transmission access, it has very serious consequences for our members, their customers, and investors. Here's what the private use rules mean in a competitive environment, which already is a reality in the wholesale market and which is becoming a reality in the retail market in nearly half of the states :

1. In its recent Notice of Proposed Rulemaking, FERC has strongly encouraged that all transmission-owning utilities participate in Regional Transmission Organizations (RTOs). Furthermore, Chairman Barton's bill and a number of other legislative proposals contemplate mandating participation in RTOs. We support the development of RTOs as important to the establishment of competitive markets that are both efficient and reliable. At the same time, private use rules may act to preclude effective participation of public systems in an RTO. A public power system that joins an RTO will not be able to issue new tax-exempt bonds to finance transmission facilities that have been turned over for operation by the RTO, thereby raising costs to all users. Moreover, a public power system that wishes to join an RTO and has issued tax-exempt bonds for transmission after July 9, 1996, will have to redeem those bonds with higher cost debt or interest on those bonds will become taxable—again, raising costs for the utility and its customers.

2. In a competitive environment, large customers will seek and obtain special tailored contracts to meet their specific needs, just as they do in buying any product. If outdated private use rules remain intact, a public power utility may be unable to offer such a contract, *even to customers in its own service territory that it has been successfully serving for decades.* This could deny that customer the best choice in the market, and will lead to loss of customers for the utility for reasons that have absolutely nothing to do with price or quality of service.

3. If a public power system loses a customer in a competitive environment (and all utilities will lose customers), the public system may be unable to re-market the generating capacity it had built to serve that lost customer as a result of the private use rules. Thus, any excess capacity that a public system has may become idle and unproductive for the economy solely as a result of the private use tax rules. Inability to resell the capacity can lead to significant financial losses and reductions in overall economic efficiency. The bottom line: the remaining customers of that utility would pay higher costs.

In summation, penalties for public power consumers come in the form of higher rates for customers, at a time when competition is supposed to be reducing rates. The consequences for public power's investors are equally undesirable. Public power's investors include a broad spectrum of people who have invested in this debt to fund their retirements, college educations, and other needs. These investors hold more than $70 billion in outstanding tax exempt debt issued to finance generation, transmission and distribution facilities, and rely on the ability of public power systems to repay them through the sale of power from the assets they financed. Failure to address private use issues places these investments in jeopardy, as it may cause downgrades of public power bonds and lead to increased turbulence in the public power debt market. This in turn may impact other segments of the municipal debt market, upon which states, cities and towns rely to finance necessary infrastructure. Uncertainty in these markets leads to higher borrowing costs, all of which ultimately will be absorbed by investors, citizens and customers.

Treatment of Private Use in the "Electricity Competition and Reliability Act"

For the reasons I have just outlined, we believe Chairman Barton has advanced the prospects for workable restructuring legislation by providing relief from private use restrictions in his bill. Chairman Barton's bill would allow publicly-owned utilities to elect to permanently forego the ability to issue future tax-exempt debt to build new generating facilities. In return, the bill would grandfather existing tax-exempt debt incurred to build electric power facilities and permit the electing systems to operate outside of current restrictive private use rules. In this way, publicly-owned utilities will be able to bring the full benefits of competition to their customers. Those utilities that do not elect to terminate issuance of tax-exempt debt would remain subject to modified private use rules.

We believe, and are pleased that Chairman Barton agrees, that a fair marketplace that invites all to participate cannot exist without meaningful relief from private use restrictions. I should note that we do have some technical concerns about a few recent modifications to the private use provisions of Chairman Barton's bill. I will be happy to address these in greater detail at the Committee's request.

Transmission Policy

I would now like to turn to transmission issues that will be important for our members in an increasingly competitive market—assuming Congress provides us with the private use relief needed to participate fully in that market. Since its inception, the LPPC has focused on transmission policy as a critical issue for its members. The LPPC was the first group of transmission owning utilities to express support for open transmission access in the debates preceding the Energy Policy Act of 1992. At the same time, we led the way in developing and promoting regional transmission entities as a mechanism to manage and operate the transmission system in an open access environment.

The LPPC would like to continue to provide leadership in making changes to the transmission system that will enhance competitive markets. As such, we would like to work with the Committee to develop transmission policies that ensure non-discriminatory access to public power transmission facilities while recognizing that it is not feasible to govern access to investor-owned and public power transmission by identical rules. We are concerned about provisions in Chairman Barton's bill that give FERC the same authority over transmission rates charged by state or local agencies as it has over private corporations. Such an expansion of FERC authority is flawed policy. By definition, State and local agencies are not private, for-profit corporations. They should not be regulated as such. For example, FERC's cost of service ratemaking methodology—which relies on concepts such as rate of return on equity—is inappropriate for public power systems whose external financing comes exclusively from debt. Also, in many instances, state and local bond covenants held by public power systems include coverage ratios that require transmission revenues in excess of the level FERC will allow under standard cost of service ratemaking.

We recommend that the Committee not give FERC general ratemaking authority over public power transmission rates. If the Committee thinks additional FERC authority in this area is necessary, it should be limited to authority to require public power systems to file the same type of open access tariff public power systems now file voluntarily under the "safe harbor" procedure used to qualify for reciprocity under Order No. 888. This new authority would be limited to requiring that public power transmission utilities offer *non-rate* terms and conditions of transmission service comparable to those that investor-owned utilities are required to offer under their open access tariffs. With respect to rates, FERC's authority would be limited to ensuring that a public power system's transmission rates are comparable to the rates it charges itself. Thus, on rates, FERC could require that public power transmission owners not discriminate in favor of their own sales services, but could not set or review such owners" revenue requirements or the level of rates. Attached to our testimony is a proposed amendment that carries out this objective.

We have similar concerns about provisions that mandate membership in RTOs. LPPC believes that an evolutionary—and not revolutionary—approach is needed to ensure the continued delivery of reliable, affordable electricity to consumers. Furthermore, as FERC has recognized, public power faces difficult issues in participating in RTOs. These must be addressed before a national system of RTOs can be put into place. As I touched on previously, private use restrictions present a barrier for participation by public power systems. Furthermore, many public power entities operate under additional legal and operational requirements that affect their ability to participate in the ownership of an RTO or to transfer ownership or operations of their transmission facilities to an RTO. These requirements include provisions in state constitutions, state and local laws, and bond covenants that vary from system to system.

For these reasons, we are unable to support any provision giving FERC authority to require public power systems to join RTOs unless in addition to addressing such issues as independence, size and scope of RTOs, the statutory criteria requires the RTO to accommodate the unique characteristics and legal requirements of public power. This will ensure that public power's participation by FERC order is not inconsistent with state laws and constitutional requirements and with bond covenant requirements. In addition, FERC RTO requirements should not impair control of local system operations or reliable and economic service to consumers served by publicly owned facilities. Lastly, the criteria should not authorize FERC to require any public power system to join an RTO if the state in which the public power system operates has chosen not to mandate that its public power entities (which are instrumentalities of the state) participate in RTOs.

Conclusion

As the Commerce Committee acts on this bill, we stand ready to offer our assistance and support to the Committee. We are hopeful that other Committee members can support the work that Congressmen Barton, Largent, Markey and others have

already done on the issue of private use. We also offer our assistance to the Committee in developing workable transmission policies that recognize the unique responsibilities and obligations of publicly-owned utilities.

As pleased and reassured as we are regarding Chairman Barton's leadership on the private use issue, I must again caution the Committee that LPPC's members will not be able to support restructuring legislation that does not provide meaningful private use relief—either in the same bill or in companion legislation from the tax committees. We recognize that the Commerce Committee's jurisdiction does not permit it unilaterally to deal with all pending tax and non-tax restructuring issues; however, we are confident that the Commerce and Ways and Means committees can work together to effectively resolve this issue.

In conclusion, the LPPC believes that the Committee continues to move in a positive direction on electric power competition issues. We look forward to working with you to ensure that private use provisions similar to those endorsed by Chairman Barton are enacted by this Congress, and through that effort, offer our assistance in supporting this Committee's efforts on broader restructuring issues, including transmission policy.

Thank you for the opportunity to testify before you today.

Mr. BARTON. Thank you, sir.

The Chair wants to announce they have just called a vote on the floor. It is on approving the journal. We are going to continue the hearing. If there is a fast member who can get over and vote and get back, I will turn the chair over, but I am going to continue the hearing.

We want to hear from our next witness, the former Congressman from the great State of Oklahoma, Mr. Glenn English, who is now representing a National Rural Electric Cooperative Association.

Mr. English, welcome to the committee. Your testimony is in the record in its entirety. We recognize you to summarize it for 6 minutes.

STATEMENT OF GLENN ENGLISH

Mr. ENGLISH. Thank you very much, Mr. Chairman. I appreciate that. Let me just say that we are very pleased to be here today and have an opportunity to address H.R. 2944.

Restructuring, we feel, brings a new responsibility to electric cooperatives around this country. It is an increasingly important option we feel that consumers will need and desire, and we want to applaud the effort by the chairman and by the committee to work with electric cooperatives to make sure that we are able to fulfill that responsibility.

Let me also say, Mr. Chairman, there are really four key items that electric cooperatives would like to focus the committee's attention on at this particular time.

While there are a number of other elements within the legislation that we address in our written testimony, and some that are of a technical nature that we would urge to be considered and looked at, the four items that we particularly want to focus the committee's attention on today deal with the guaranteed right of consumers to aggregate and right of electric cooperatives to serve those consumers; second, to minimize the unnecessary regulatory burdens on consumer-owned electric cooperatives; third to put all electric utilities in the same ball park as far as the services that they can offer to consumers; and fourth, we want to permit electric cooperatives to work together to serve consumers more efficiently.

The first issue with regard to the right to aggregate, we want to commend the chairman for the legislation and his addressing of

this issue. We feel that certainly the legislation moves in the right direction as far as dealing with that particular concern.

The second issue, the summary signal, that the intent was for electric cooperatives with limited transmission facilities to be able to, in an uncomplicated way, obtain exemption from the jurisdiction of the Federal Energy Regulatory Commission. We feel that is a very laudable intent by the legislation, since there are some 400 small electric distribution cooperatives who use high-voltage lines to provide retail service to their widely disbursed rural consumers.

Now, these facilities have no impact—I want to repeat, no impact—on the transmission grid, and for that reason should not have to undergo any type of expensive or prolonged regulation by the Federal Energy Regulatory Commission.

With that in mind, we would urge the chairman and the committee to work on the language, itself, to clarify the issue and to state in detail, if possible, a simple, inexpensive exemption process to provide the small distribution cooperatives with the kind of certainty that they are going to need in dealing with the process.

Let me also say, Mr. Chairman, we took note of the fact that the Federal Energy Regulatory Commission is authorized to review mergers not only among the large entities, the mega-mergers of this country, but between cooperatives, as well.

We were somewhat puzzled by that inclusion in the language of the legislation, quite frankly, because these are, for the most part, small entities.

In fact, when FERC needs to be focusing its attention on the mega-mergers that are taking place and the impact that that is going to have as far as consumers around this Nation, it appears that this is diverting resources and attention to deal with people who have little or no impact as far as the market power issues of this country are concerned.

In particular, we have been calling for even a heavier review of some of these mega-mergers that have been taking place in this Nation, and we still feel that the bill unduly restricts FERC's authority to look at those mega-mergers.

In particular, from a size standpoint, Mr. Chairman, to make my point about the fact that this is somewhat puzzling, if you took all the generation and transmission capabilities of all electric cooperatives all across this country and merged the whole group together, they still would not be as large as the American Electric Power Company's assets.

Second is the fact that these electric cooperatives generate power for their own use for their own membership. If you take all the electric generation capability that we have among our membership, it still only covers about half of all the electric power needs of individual cooperatives. Since nearly all that is committed to our membership, it really does not leave much available for any of our members who may wish to become players in an open market to be much of a factor, so that really does not make much sense.

The other thing that I would call to the committees attention, mergers by rural electric cooperatives, G&Ts, are already under review by the Rural Utilities Service. Any of those that have an RUS loan are required to undergo review and approval before they can

take that action, so there is already Federal review at that particular point.

To simply add the Federal Energy Regulatory Commission is an additional burden on electric cooperatives as a second review at the Federal level, and also as a diversion of much-needed resources for the Federal Energy Regulatory Commission to be focusing on what is the real issue, and that is the mega-mergers and the market power that is going to truly have an impact on the marketplace in this country.

We would like to work with the committee to see if there is some way we can address this issue, and to deal with the fact that cooperatives that are small and self-power primarily are the only members, and other cooperatives already subject to Federal merger could not be dealt with.

Mr. Chairman, I see my time has expired. I do want to address several other issues, but I hope to be able to do that during the question period, and particularly I would like to address the issues pertaining to propane. Some of the issues have been raised of our good friends of the propane industry regarding subsidies and taxes.

Thank you, Mr. Chairman.

[The prepared statement of Glenn English follows:]

PREPARED STATEMENT OF GLENN ENGLISH, CHIEF EXECUTIVE OFFICER, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

INTRODUCTION

Chairman Barton and Members of the Committee, I appreciate this opportunity to continue our dialogue on the restructuring of the electric utility industry. For the record, I am Glenn English, CEO of the National Rural Electric Cooperative Association, the Washington-based association of the nation's nearly 1,000 consumer-owned, not for profit electric cooperatives.

These cooperatives are locally governed by boards elected by their consumer owners, are based in the communities they serve and provide electric service in 46 states. The more than 32 million consumers served by these community-based systems continue to have a strong interest in the Committee's activities with regard to restructuring of the industry.

Electric cooperatives comprise a unique component of the industry. Consumer-owned, consumer-directed electric cooperatives provide their member-consumers the opportunity to exercise control over their own energy destiny. As the electric utility industry restructures, the electric cooperatives will be an increasingly important option for consumers seeking to protect themselves from the uncertainties and risks of the market. I would like to thank you, Mr. Chairman, and Members of the Committee for your receptiveness to the concerns and viewpoints of the electric cooperatives.

The title of the bill before the Committee, H.R. 2944, is The Electricity Competition and Reliability Act. We applaud the intention of the Chairman and the Committee to ensure true competition in the electric utility industry. We are evaluating each provision of the bill on the basis of whether it enhances or impedes competition, and whether it supports or impedes the ability of electric cooperatives to continue to meet the needs of our consumer-owners in that restructured industry.

At the beginning of my testimony, I would like to focus on a few key issues that we believe must be addressed if NRECA is to be able to support H.R. 2944. In the second part of this testimony below, I will discuss a number of other elements in the bill about which we are concerned. We intend to continue to work with the Committee and Congress to try to address those issues. In the third part of my testimony I will also note a few simple changes we recommend to fix technical problems in the bill.

KEY PRIORITIES

NRECA and the electric cooperatives seek legislative language that would guarantee consumers access to the "cooperative option." We were looking to see if H.R. 2944 would:

- guarantee consumers the right to aggregate and the right of electric cooperatives to assist those aggregation groups;
- minimize unnecessary regulatory burdens on consumer-owned electric cooperatives;
- put all electric utilities on an level playing field with respect to the sale of non-electric products or services; and
- permit electric cooperatives to work together to serve their consumers more efficiently.

On the first issue, the discussion summary of "Major Changes" released last week indicated that the Chairman's intention in H.R. 2944 would be to clarify the authority of cooperatives to aggregate retail customers.

And, we were pleased to see, the language of H.R. 2944 does, indeed, clarify the authority of cooperatives to aggregate retail consumers.

On the second issue, the summary signaled the Chairman's intention to give distribution cooperatives with limited transmission facilities—utilized only for the distribution of electric service—an uncomplicated way to obtain an exemption from the jurisdiction of the Federal Energy Regulatory Commission (FERC).

This is a laudable intent. More than 400 small electric distribution cooperatives use high voltage lines to provide retail electric service to their widely dispersed rural consumers. These facilities have no impact on the transmission grid, and should not be subject to expensive, unnecessary FERC regulation.

We were disappointed to see, however, that the language of H.R. 2944 was not consistent with the discussion summary. Although the summary described an uncomplicated self-certification process to exempt these distribution cooperatives from FERC jurisdiction, H.R. 2944 subjects these small distribution cooperatives to a complicated and uncertain process that does not accomplish the Chairman's goal.

Congress should not use FERC regulation as a barrier to small cooperatives and new entrants into the market place. We believe it is possible to create a simple, inexpensive, exemption process that provides small distribution cooperatives with the certainty they need.

On this same issue, we were concerned that both the discussion summary and the bill language would authorize FERC to review mergers between cooperatives.

In previous testimony before this Committee and the House Judiciary Committee, NRECA has expressed concern that mega-mergers in the electric utility industry could lead to undue market concentration that would harm competition, reduce the quality of electric service, and raise prices for consumers. For that reason, we welcomed the bill's restoration of FERC authority to review public utility mergers. And, as I discuss in the second section of this testimony, below, we are concerned that the bill still unduly restricts FERC's ability to review these mega mergers.

At the same time, however, we are concerned that the bill also requires cooperatives to obtain FERC approval before they can merge. I want to emphasize the unnecessary burden that this provision imposes on electric cooperatives and their member-consumers without providing any benefit to the objectives of the legislation.

Of course, we recognize the Committee's wish for a uniform approach to merger review, but there are legitimate differences that the Committee needs to recognize between mega mergers that could harm the development of competition for electric energy and mergers between small, member-owned electric cooperatives.

First, because of their small size and member-focus, mergers between cooperatives simply do not have the same impact on the competitive market as do mergers between large investor-owned utilities. If all of the generation and transmission cooperatives were merged into one national entity, that entity would not be as large as AEP—American Electric Power.

Moreover, cooperatives are selling most of the power they produce to their own members because they were formed to bring their members a reliable, affordable source of power, not to speculate in open markets or to make a profit. Even if they wanted to get involved in the open market, most generation and transmission cooperatives could not. Nationally, generation and transmission organizations generate only about half of the electricity required by their member systems. They do not have the uncommitted or merchant power supplies required to become major players in energy markets.

Second, mergers between cooperatives are also already subject to extensive review. Any merger of electric cooperatives requires the approval of their member-owners. And, any merger involving a cooperative with outstanding Rural Utilities Service (RUS) financing is subject to comprehensive review by RUS.

Instead of protecting the public interest, FERC review of cooperative mergers only makes it more difficult for cooperatives to meet their obligation to meet the power supply needs of their member consumers at the lowest possible cost. And, because of their small size, there are times when cooperatives can operate more efficiently,

acquire power at lower costs and reduce market risks for their members by joining with their neighboring cooperatives.

Congress should be encouraging consumer-owned electric cooperatives to work together to provide better service for their member-consumers, not subjecting them to new regulatory burdens.

We would like to work with the Committee to draft an exemption from FERC merger review for those cooperatives that are small, sell power primarily to their own members and other cooperatives, or are already subject to federal merger review.

The second issue I want to raise today is the need for Congress to provide some consistency with respect to the non-electric businesses in which sellers of electric energy can engage.

Today, investor-owned utilities, municipal utilities, electric cooperatives, power marketers, and other participants in the retail electric market are subject to different limitations on their ability to participate in the market for non-electric products and services. Those differences are unbalancing the playing field in the electric energy market and increasing costs for consumers.

More and more, competitors in the electric energy market will be attracting consumers by offering packages of products and services. Consumers may be buying their electric energy, their natural gas or propane, their cable television, and their local telephone service from the same company.

If one class of participants in the electric energy industry is denied the right to offer services that other participants can offer, it will be unable to meet the needs of consumers interested in packaged offers. So limited, that class of participants will be at a distinct disadvantage.

We would like to work with the Committee to draft language that would ensure that all participants in the electric energy industry are on an equal footing. Such language would not give sellers or distributors of electric energy the right to sell any particular product or say that states have to allow any seller or distributor of electric energy the right to sell any other product or service. All it would say is that states have to treat all providers equally.

This language is particularly important if Congress chooses to repeal PUHCA. Proponents of PUHCA repeal have argued that it makes no sense to impose artificial restrictions on the lines of business that certain utilities can engage in based solely on the form of those utilities" corporate structure. That logic applies here as well.

Now, you are probably already hearing from some who are pressing for restrictions on cooperatives. In recent weeks, for example, a number of propane gas spokesmen and their hired Washington-based lobbyists have circulated misrepresentations on Capitol Hill, charging electric cooperatives with unfair competition in the provision of propane service.

These spokesman claim that cooperatives utilize low-interest funding from the Rural Utilities Service to set up propane companies that compete unfairly by selling propane at "below market" prices, and that cooperatives are able to do so because those propane operations are "cross-subsidized."

Let me put that notion to rest right here and now. Electric cooperatives may not, by law, cross-subsidize a subsidiary organization, be it propane, provision of water and sewer utility services, Internet access, satellite television service or home security services. All costs of subsidiaries are allocated to those subsidiaries or those subsidiaries are operated with separate staff and facilities.

Electric cooperatives that enter the propane business generally enter because their consumers request it or because existing small propane organizations approach the cooperatives to take over the business. The resultant propane businesses operate to recover costs, not profits, and their rates reflect that.

Some charge that cooperatives providing diversified services are able to compete at an advantage because they "don't pay taxes." It is true that most cooperatives pay no federal income taxes on their electric business because they are tax-exempt companies and because they operate on a not-for-profit basis. But, when cooperatives engage in most diversified businesses, they must pay unrelated business income tax on any profit they make from those businesses. Moreover, if the cooperatives pass any revenue from those diversified businesses to their consumer-owners as dividends, the cooperatives" members must pay income taxes on those dividends.

Further, cooperatives and their subsidiaries pay every other business, personal property, transaction, sales, or other tax that every other business entity pays.

I just wanted to make that clear. Cooperatives are different from corporations and proprietorships and partnerships in a number of ways: they are organized by and for consumers; they operate as non-profit entities; their sole focus is the provision of services to their consumers and responding to requests for services from those

consumers. In the realm of state and local taxes, though, they are exactly the same as every other business.

This is important to bear in mind in the restructuring of the electric utility industry. Because cooperatives are consumer-owned and consumer-driven organizations with a history of success in providing services, consumers look to their cooperatives to provide additional services necessary for the their communities. Limitations on the ability of cooperatives to continue to provide these services, to provide services that every other electric utility can provide is a restriction on the ability of consumers to provide for themselves.

The last issue I want to focus on today is the need for electric cooperatives to work together to meet consumer needs.

Let me give you an example. In Georgia, electric cooperatives serve a number of Kroger supermarkets. Kroger, for reasons of efficiency, wishes to receive one bill for the electric service for all of its stores.

When Georgia moves to competition, a single large power marketer or investor-owned utility could probably provide that service directly. It would have the geographic scope and resources to be able to do so. But it would not have any local relationship with the individual Kroger stores or the communities in which they operate.

On the other hand, the several electric cooperatives now serving the Kroger markets do have that long standing relationship with the stores and their communities. But, because more than one cooperative would have to work together to provide a common service, they might not be able to provide that consolidated bill directly without violating federal antitrust laws.

Instead, they would have to expend the resources to organize a joint venture specifically to provide that service. And even so, they could inadvertently violate federal antitrust law.

Federal antitrust law was just not written with consumers or cooperative consumer organizations in mind, and the law sometimes gets in the way of common sense. The kind of cooperation that could better serve consumers—in this case, both Kroger and the cooperatives other members—was not contemplated by the law.

I recognize that this is not the jurisdiction of this Committee, but I also recognize the Committee's interest in all of the issues related to true competition in the electric utility industry. I'm not suggesting that cooperatives be exempt from antitrust provisions. I am pointing out to the Committee that the competitive bar is higher for small entities than it is for large, interstate and international utilities.

ADDITIONAL AREAS OF CONCERN

While the three issues emphasized above are NRECA's key priorities, there are a number of other issues in the bill that are of concern to electric cooperatives and their members. As this bill moves through the legislative process, we intend to continue to work to address these issues. For the convenience of the Chairman and the Committee, I'd like to discuss these matters sequentially as they appear in the bill, rather than in any priority order.

Findings

H.R. 2944's ninth finding states:

> Federal programs to benefit rural consumers have succeeded, and rural America has been electrified. However, rural America pays some of the highest electric rates in the country. Competition will assure reliable, reasonably priced rural electric service.

This finding is inaccurate. Rural America pays high electric rates because it costs more per consumer to provide distribution service, not energy. To serve their members, rural utilities must string far more wire and cross far more rugged country than the suburban and urban utilities. Rural electric cooperatives serve an average of 5.76 consumers per mile of line. By contrast, investor-owned utilities average 34.85 consumers per mile of line and municipal utilities average 47.76 consumers per mile of line.

Restructuring will only bring competition to sales of electric energy, not distribution or transmission. Thus, even if competition lowered energy costs, it would not have any effect on distribution costs, the largest contributor to rural consumers" high energy costs.

There is also significant question whether restructuring will bring benefits to rural consumers. A draft study by the Department of Agriculture, and studies completed by the American Gas Association, the Competition Policy Institute, and several universities have all found that competition could actually raise rates in rural communities and largely rural states.

Experience in states that have already restructured also cast doubt on this Finding. Pennsylvania has often been touted as the state whose electric restructuring efforts have brought choice to the most consumers. To take advantage of that choice, Pennsylvania's electric cooperatives opened up their systems ahead of schedule to allow every one of their members the right to choose his or her electric supplier. Yet, there is not one alternative supplier of electric energy today willing to offer competitive service to those cooperatives" members. The benefits of competition have not reached Pennsylvania's rural communities.

Regional Transmission Organizations

NRECA has several concerns with § 103 of the bill concerning regional transmission organizations (RTOs)

Mandatory Participation

NRECA has long been supportive of voluntary RTOs. As NRECA has stated in its comments on FERC's Notice of Proposed Rulemaking on RTOs, NRECA believes that properly designed RTOs can provide significant system benefits, increasing reliability and reducing the ability of transmission owners to exercise market power.

Mandatory RTOs, however, as provided by H.R 2944, pose several risks to the reliability of the system and to the healthy operation of energy markets. We hear from our members that the only thing worse than no RTO is a bad RTO. An RTO put together too fast, without full agreement of all industry participants and without adequate review from FERC is a prescription for problems. A bad RTO can make it easier for transmission owners to exercise market power, to favor their own generation, to restrict the flow of power across the RTO, or to raise transmission prices unreasonably. By mandating the formation of RTOs at short notice, and by restricting FERC's ability to regulate the structure, type or form of an RTO, the language now in H.R. 2944 could make the formation of bad RTOs far more likely.

Independence

We are pleased that the standards for regional transmission organizations in § 103 of the bill require RTOs to be independent of all market participants. We are concerned, however, that H.R. 2944 requires FERC to accept as "independent" RTO structures that we believe could continue to allow large utilities to exercise undue control over their transmission facilities. That could require FERC to accept RTOs that retain, or even exacerbate, existing problems with reliability and market power.

Moreover, pursuant to its Notice of Proposed Rulemaking on RTOs, FERC is currently holding a public process to develop appropriate standards for RTOs. All interested parties, including utilities, consumers and even Wall Street, are now filing comments and reply comments with FERC. Among other issues addressed in those comments is the appropriate definition of "independence." H.R. 2944's definition prejudges that process and imposes its own definition in the absence of a public process.

We would like to see the definition of "independence" deleted from § 103 of the bill.

Incentive Pricing

We have a similar concern with respect to the subsection in the bill addressing "Incentive Transmission Pricing Policies." That section requires FERC to encourage incentive transmission pricing policies for RTOs. As with the issue of "independence," appropriate pricing policies for RTOs is currently subject to public debate at FERC. The issue has arisen not only in the context of the RTO Notice of Proposed Rulemaking, but also in the context of at least one pending case on an individual RTO's rates.

Again, we think that H.R. 2944's provision has inappropriately pre-judged the proper result of an ongoing public process. We would like to see the standards in this section made voluntary for FERC so that FERC is free, when it has completed its current investigation, to apply the rule that it finds most likely to serve the public interest.

Electric Reliability

I would like to thank the Chairman and the Committee for including in H.R. 2944, with only minor amendments, the electric reliability language that was adopted by the NERC Board of Trustees. NRECA, and a coalition of other industry participants, believe that the language adopted by the NERC Board comprises the best option now possible to provide for the continued reliability of the bulk power system.

Rather than express concerns with the language in the bill, I would instead ask the Committee to resist requests to further amend the language. There are those

who oppose certain aspects of the language, or who would like a greater say in the operation of the electric reliability entity or the bulk power system than the language allows, and NRECA and the coalition are continuing to talk to those interests to see if a compromise can be worked out.

We respectfully request that the Committee not make further changes to the reliability language until that group can reach agreement. Otherwise, the fragile consensus that has developed within the industry on the NERC language could dissipate, and result in failure to enact much needed legislation to preserve reliability.

Mergers

As I mentioned in the main part of my testimony, NRECA is very pleased that H.R. 2944 restores FERC merger review. As I have testified to before this Committee and the House Judiciary Committee, unfettered mega-mergers in the electric utility industry pose a significant threat to the development of competition in the industry.

Unfortunately, while H.R. 2944 does restore FERC merger review, it also appears to reduce the opportunity for public scrutiny of mergers and to hamper FERC's ability to protect the public interest.

First, H.R. 2944 replaces the current hearing process with a simple comment period. By doing so, H.R. 2944 reduces the transparency of the merger review process and denies FERC and the public the access to information they need to properly evaluate the potential competitive impact of the proposed merger.

Second, H.R. 2944 also establishes strict deadlines that would hamper FERC's ability to thoroughly review large utility mergers. Some of these mergers involve international companies with hundreds of subsidiaries and affiliates, billions of dollars of assets in a dozen or more states, and millions of consumers. The time limits imposed by H.R. 2944 would not give FERC sufficient time to evaluate the impact that such mergers would have on the $220+ billion electric industry.

NRECA continues to believe that it is in the public and consumer interest for FERC to have full authority to conduct a public review of mega-mergers between public utilities that could eliminate or limit competition in the marketplace.

The Committee should understand that electric cooperatives do not oppose all utility mergers. Mergers can be a legitimate business strategy to respond to changing markets and changing market conditions. Since 1996, FERC has given its blessing to approximately 30 utility mergers and many more are pending. NRECA has requested hearings in only two of those proceedings.

In fact, NRECA has supported the application of loosened review requirements for mergers between smaller entities that could increase competition in the market place by creating a new company that can compete more effectively without being large enough itself to exercise market power.

NRECA would be happy to work with the Committee and Congress to develop language that would achieve the proper balance between protection of the public interest and the encouragement of efficiency in the industry.

Public Utility Holding Company Act of 1935

As I have said in previous testimony, NRECA believes that it is a mistake to repeal the Public Utility Holding Company Act of 1935 (PUHCA). PUHCA protects both electric consumers and competition in the electric utility industry by helping to ensure that public utilities do not grow too large or complex to be effectively regulated.

If the Committee nevertheless intends to go forward with PUHCA repeal, NRECA strongly urges the Committee to consider the approach taken in the bill sponsored this Congress by Representatives Steve Largent (R-OK) and Ed Markey (D-MA), which takes a sensible approach. Their proposal would repeal the consumer protections in PUHCA only for those utilities that operate in states where competition has already been implemented. That approach would provide competition a better chance to put down roots and start to grow before any public utilities were freed from PUHCA's protective provisions.

Interconnection

NRECA recognizes that the development of new distributed generation technologies and the interconnection of such facilities to the grid are increasingly important. Cooperatives have made extensive use of existing distributed generation technologies and have been actively working to study new distributed generation technologies and to develop new applications where distributed generation can improve reliability and lower costs for consumers.

Cooperatives have also been involved in parallel efforts to develop standards for the interconnection of distributed generation technologies with the grid. One is being conducted by the Institute of Electrical and Electronic Engineers and the

United States Department of Energy (DOE). The other is being conducted by the National Association of Regulatory Utility Commissioners (NARUC) and is funded by the DOE. Just this week, NRECA submitted comments on a Draft Report to NARUC on interconnection issues.

Nevertheless, NRECA is concerned that the substantive provisions of § 542 of H.R. 2944 could impose unnecessary costs on electric utilities and their consumers. Moreover, the section's requirement that FERC develop interconnection standards is probably premature. It would likely preempt the efforts now pending before the Institute of Electrical and Electronic Engineers and NARUC, and the tight deadline could require FERC to act before it or the industry fully understands the effects that developing distributed generation technologies will have on the safety and reliability of the interconnected grid.

Other PMAs

NRECA is concerned that § 632 of H.R. 2944, "Wholesale Power Sales By Federal Power Marketing Administrations," gives FERC the unnecessary and inappropriate authority to change rates set by the power marketing administrations.

Today, the PMAs are required to set their rates to recover their costs, as those costs are defined by Congress. They propose their rates to the Secretary of Energy who then submits them to FERC for review. Because the PMAs rates must be set according to very specific statutory requirements, FERC does not today have the authority to modify the PMAs rates. Instead, if FERC is concerned about something in the rates, it can only reject the rates and remand them to the PMAs. That ensures that the final development of the rate is set by the regulatory entity most familiar with the costs that have been recovered and the statutory mandates with regard to the rates.

We would like to see all of § 632 deleted.

Net Metering

Section 702 of H.R. 2944 requires retail electric providers to make net meters available to consumers that have installed eligible on-site generating facilities. NRECA believes that net metering imposes an unreasonable obligation on electric consumers to subsidize those who install self-generation.

The policies require utilities to pay consumers retail price for wholesale power. That is an even higher subsidy than the "avoided cost" price provided by PURPA. The policies also require utilities to pay high costs for what is generally low-value power. Power from wind and photovoltaic systems is intermittent, cannot be scheduled or dispatched reliably to meet system requirements, and is expensive to integrate into the system.

Further, net meters cause customers to under pay the distribution and other fixed costs they impose on the system. A utility has to install sufficient facilities to meet the peak requirement of the consumer and recovers the costs of those facilities through a kWh charge. When the net meter rolls backwards, it understates the total kWh consumed by the customer, and thus under recovers the utility's costs.

Finally, net meters can be deliberately or inadvertently "gamed." Consumers with self-generation can lean on the system by drawing power at times when it is expensive for the utility to provide it and then run down the meter by self-generating at times when the utility does not need the power. That can be a problem with windmills particularly because wind is often calm in the hot times of day when system demand peaks, and then picks up again in the cool evenings when system requirements are low.

Environmental

We are pleased that Section 701 of H.R. 2944 was revised from the discussion draft to ensure that the Renewable Energy Production Incentive (REPI) program is available only to not-for-profit electric cooperatives and municipally-owned entities that generate electric energy for sale using solar, wind, biomass or thermal energy. In addition, we applaud deletion in H.R. 2944 of a cap of $50 million through 2004, which had appeared in the discussion draft.

Internal Revenue Code

While the 85/15 tax issue is addressed in H.R. 2944, it falls short of what is needed to address issues raised in a restructured electric utility marketplace. For example, the language fails to address revenue from unbundled electric activities (including metering, billing and service charges), revenues from asset sales, and revenue from diversified businesses provided the business is operated on a cooperative basis.

TECHNICAL ISSUES

In addition to the substantive issues discussed above, there are a few technical fixes that need to be made to ensure that the language in the bill actually achieves its intended purposes.

Public Purpose Charges

Section 101(d) of the bill provides that it does not affect the authority of a State or municipality to require public purpose charges. The section serves an important purpose, but appears to leave out some electric cooperatives.

There are three categories of electric utilities that may need to collect public purpose charges. The first—state-regulated electric utilities—includes all investor-owned utilities and a few cooperative utilities that operate in states where they are subject to state regulation of their rates. The second category is municipal utilities, who are not regulated in most states. The third category is cooperatives who, like municipal utilities, are not regulated in most states. Section 101(d) takes care of the first two categories, but not the third: non-state regulated cooperatives.

We would be happy to suggest to the Committee a very simple fix to address this oversight.

Definition of Transmitting Utility

Section 102(d) of the bill includes a new definition of transmitting utility. It has been amended to include utilities that own transmission not used for wholesale sales. In H.R. 2944, an additional parenthetical has been added at the end that has not appeared in prior drafts: "(other than facilities subject to an order of the Commission under section 210 or 211)."

That parenthetical appears to be a partial transposition of language in the definition of "public utility" that states "other than facilities subject to such jurisdiction solely by reason of section 210, 211, or 212."

The parenthetical creates a cyclical definition problem. Sections 210 and 211 apply to transmission facilities owned by transmitting utilities. If "transmitting utility" does not include entities that own facilities subject to §§ 210 and 211, then there are no transmitting utilities.

Reciprocity

Section 501 of the bill provides for retail reciprocity. It attempts to ensure that any utility that seeks to compete for other utilities" consumers provides its own consumers with choice. In order to prevent efforts to bypass the reciprocity provision, the bill also applies to entities affiliated with electric utilities.

NRECA believes that Congress should not have to mandate reciprocity requirements. A national mandate inappropriately imposes rules on those individual states that believe their consumers interests are better preserved through open competition than through reciprocity requirements.

Rather than focus on the merits of a reciprocity requirements, however, I would rather ask this Committee to make a technical fix to the section that should eliminate some unintended consequences of the bill.

As drafted, the provision applies to "affiliates," but the term "affiliate" is not defined in the Federal Power Act. It is unclear, therefore, how the section will be applied. Depending on a court's interpretation of "affiliate," the provision could either be too broad, or too narrow.

For example, under one definition of "affiliate," it would only include two companies, one of which owns an interest in the other. Under this definition, "affiliate" would not apply to two companies with common ownership. A utility could therefore evade the reciprocity requirements by creating a holding company and put power marketing and distribution functions in two sister subsidiaries.

On the other hand, "affiliate" could be interpreted broadly to include any two companies that share significant interests, in each other, or in a third company. FERC has adopted this interpretation of affiliate in certain contexts. Under this definition, there is a risk that two cooperatives that each have an ownership interest in a common generation and transmission utility could be considered affiliates. If that happened, the reciprocity provision could prohibit a cooperative in one state from competing for consumers in that state because the cooperative's G&T also served a cooperative in other states that had not moved to competition. The reciprocity provision could apply even though the two distribution cooperatives involved had no ownership interest in each other and no common owners.

We would be happy to work with the Committee to insert a definition of "affiliate" that would eliminate the potential for over inclusiveness or under inclusiveness.

CONCLUSION

Mr. Chairman, all of us harbor many concerns regarding the restructuring of this basic, essential, complex industry. The Committee and you—in particular—Mr. Chairman, have been attentive and receptive to the concerns of 30 million electric cooperative consumers.

This bill does not contain everything that electric cooperatives would like to see in a restructuring bill. We have outlined some of those concerns as an attachment to my testimony. We will continue to work with the Committee and with the Congress to ensure that electric cooperative concerns are met. That is how the legislative process works. Given the discussions that we have had with you, Mr. Chairman, and with the Committee, we are confident that some of these concerns will be worked out, and that the intentions of the discussion summary will be clarified in final bill language, and on the basis of that, electric cooperatives do not object to moving this bill forward.

It is, of course, possible that proposals to change this legislation will make parts of it totally unacceptable to electric cooperatives, and in that case, we would have to oppose those changes and, possibly, the legislation. Again, that's the way the legislative process works.

I appreciate the opportunity to discuss H. R. 2944 and these very important matters with the Committee today. Electric cooperatives will continue to be available to the Committee to bring true competition to the electric utility industry and to ensure that the benefits of that competition flow equitably to all electric consumers.

I would be happy to answer any questions.

Mr. BARTON. Thank you, Mr. English.

We now want to hear from Mr. David Hawkins, who is the director of air and energy programs at the Natural Resources Defense Council.

Your statement is in the record in its entirety, and we would recognize you for 6 minutes to summarize.

STATEMENT OF DAVID G. HAWKINS

Mr. HAWKINS. Thank you, Mr. Chairman.

I would like to make two points this morning. The first is that we have a huge remaining air pollution problem from electric generating in this country, and the second is that we should address that problem as part of a restructuring program.

First, the nature of the air pollution problem. Contrary to expectations some 30 years ago when Congress first expressed itself on controlling pollution from electric generation and their sources, many existing power plants that were in operation 30 years ago are still in operation, and they are still operating under outmoded pollution control rules and not meeting modern environmental performance standards, and yet they are competing against facilities that are required to meet modern environmental performance standards—in our view, competing unfairly.

But first the environmental issue. The electric generating industry, as a result of these policies, these flawed policies, is the single largest sector that is responsible for some of the most pervasive remaining air quality problems in this country.

Electric generating is responsible for over two-thirds of the Nation's sulfur dioxide emissions, and around a third of nitrogen oxides, mercury, and carbon dioxide.

Now, these pollutants are responsible for what we call a Pandora's Box of health and environmental harm. They are responsible for fine particles that contributes to tens of thousands of premature deaths in the U.S. each year; smog that plagues our major cities and causes respiratory attacks in children and in seniors; acid rain that still damages lakes, streams, forests, and monuments; regional

haze that spoils trips every year for millions of people who visit our national parks; nitrogen emissions that help over-fertilize productive estuaries, including the Chesapeake Bay, Long Island Sound, Pamlico Sound, and Pamlico Sound, and the Gulf of Mexico, leading to dead zones where aquatic life perishes; and mercury contamination of lakes and streams that has led over 40 States to issue continuing advisories against the consumption of fish that store this toxin; and, finally, carbon dioxide—the pollutant that you cannot get away from—carbon-dioxide-driven climate change that threatens to create disruptive weather patterns and sea level rise that modern human civilization simply have never experienced.

The second point is: why address these issues now?

First, delaying addressing these issues is not going to make Congress' job any easier. These issues will have to be addressed, and they will not get easier by simply trying to brush them away right now. What it would do is increase the environmental damage associated with delay, and also prolong uncertainty.

Second, a failure to address today's balkanized emission rules will leave in place an industry structure where fair competition is simply not possible.

Today, the amount of pollution resulting from producing a megawatt hour of electricity varies widely from State to State. Nitrogen oxide emissions in States range from below two pounds per megawatt hour to over eight pounds per megawatt hour. Sulfur dioxide emissions range from below four pounds per megawatt hour produced to a high of over 20 pounds per megawatt hour.

Now, these policies are a direct result of the patchwork of regulations that, in effect, operate as a subsidy to dirtier generators.

Because all markets are connected by wires, different pollution standards promote a survival of the filthiest market, where plants that are the dirtiest bid power at the cheapest prices and are able to increase their market share.

But these market distortions really do not deliver large consumer benefits. The price differences caused by different pollution requirements are quite small, usually on the order of 2 to 3 mills per kilowatt hour or less. But these small differences in a competitive marketplace are enough to give dirtier producers a decisive market advantage in many areas.

A generation performance standard would be a reform that would create a level playing field for generators. The standard would define the amount of pollution that could legally be emitted for a kilowatt hour of electricity and would treat all players fairly, and it would directly reward cleaner, more-efficient generators and remove the subsidy that current policy provides to dirtier ones.

Congressman Pallone's Fair Energy Competition Act, H.R. 2569, contains such an approach and we support it.

A final benefit of setting the environmental ground rules for this industry is that it would provide a clear road map for business in planning long-term investments. The history of the clean air program has developed as a series of unconnected initiatives, typically focused on a single pollutant. Today, we can look over the next 10 to 15 years and realize there will be a number of additional environmental problems that will have to be addressed. But if we pursue the traditional approach, no one can say with certainty which

pollutants will be addressed first, how deep the reductions will be, and in what order the steps will occur.

As a result, business planners today must approach their investments by making educated guesses about future environmental requirements.

Billions of dollars are changing hands as generation plants are sold under State restructuring programs. One thing we can say for sure is someone is guessing wrong.

By enacting integrated cleanup programs, Congress could provide both certainty and reduce the tendency to prolong dependence on existing, outmoded plants through the traditional process of applying end-of-the-pipe cleanup devices normally aimed at controlling only one pollutant.

Now, the chairman and the ranking member's State, Texas, has recognized the value of addressing both of these issues together, and recently enacted legislation in Texas has addressed air pollution directions as part of a cleanup program. We commend that example to the committee, but point out that no State can solve its problems alone; hence, the need for Federal policy.

Thank you.

[The prepared statement of David G. Hawkins follows:]

PREPARED STATEMENT OF DAVID G. HAWKINS, DIRECTOR, AIR & ENERGY PROGRAMS, NATURAL RESOURCES DEFENSE COUNCIL

ELECTRICITY GENERATION AND AIR POLLUTION

Today, electric generation imposes an enormous burden of air pollution on the American public and the great bulk of that pollution comes from plants that are not required by federal, state, or local policy to meet technically feasible, affordable modern environmental performance standards. This policy failure stems from decisions made in Congress nearly thirty years ago.

In the 1970 Clean Air Act Congress required that all new powerplants and other large pollution sources be designed to minimize air pollution using state-of-the-art techniques. But the Act exempted existing plants from this performance requirement. Instead existing plants, if controlled at all, were required to clean up only to the degree needed to address local air quality problems.

There were several reasons for this approach. First, most air quality problems were perceived as local. Second, at the time, the electric power industry was mostly a local one. Third, the exemption was assumed to be temporary—Congress believed existing plants would retire and be replaced by new ones meeting modern performance standards.

Now, nearly 30 years later, we know that the facts on the ground have changed. We know now that many of our most threatening air pollution problems are not local—they are regional, national, and even global. Our electric generating industry is rapidly becoming a national industry with all parts of the country connected by wires over which the product can move anywhere in the lower 48 states. And those powerplants that were supposed to retire have kept on running like the Energizer Bunny. As a result, pollution from electric power generation is a dominant cause of nearly all our most pressing air quality related problems.

Four pollutants cause a host of public health and environmental damage: sulfur dioxide, nitrogen oxides, mercury, and the pollutant no one can get away from, carbon dioxide, the dominant greenhouse gas. Electric generation in the U.S. is the largest single source of these four horsemen of air pollution. Electric powerplants release over ⅔ of total U.S. emissions of sulfur dioxide, and over ⅓ of each of the other three pollutants. These pollutants are responsible for a Pandora's box of health and environmental harm:

- fine particles, that contribute to tens of thousands of premature deaths in the U.S. each year;
- smog that plagues our major cities, and causes respiratory attacks in kids and seniors;
- acid rain, that still damages lakes, streams, forests, and monuments;
- regional haze, that spoils trips to national parks for millions of visitors annually;

- nitrogen emissions that help over-fertilize estuaries, including the Chesapeake Bay, Long Island Sound, Pamlico Sound, and the Gulf of Mexico, leading to dead zones where aquatic life perishes;
- mercury contamination of lakes and streams that has lead 40 states to issue continuing advisories of the fish that store this toxin;
- and, carbon dioxide driven climate change, that threatens to create disruptive weather patterns and sea-level rise that modern human civilizations have never experienced.

This plague of pollution problems is a product of the grandfather loopholes in current federal law that allow 30, 40 and 50-year plants to keep operating without meeting modern performance standards. The patchwork of lenient or nonexistent rules at the state and local level has created pollution havens where grandfathered plants can engage in domestic environmental dumping, distorting fair energy markets.

As we move to modernize the electricity market economically, we must accompany it with modern environmental performance measures. A central purpose of electric industry restructuring legislation is to create a free and fair, competitive market for energy services. But fair competition is impossible in an environment where air pollution performance requirements are balkanized. Because all markets are connected by wires, different pollution standards promotes a "survival of the filthiest" market, where plants that are the dirtiest bid power at the cheapest prices and increase their market share.

These market distortions do not deliver consumer benefits. The price differences caused by different pollution requirements are quite small—usually 2-3 mills per kilowatt-hour or less—but these small differences are enough to give dirtier producers a decisive market advantage in many areas. The market distortions also discourage investment in new, cleaner, more efficient generation and in renewable resources.

Under the current rules, an entrepreneur who seeks financing for, say, a clean, high-efficiency natural gas plant can point out that it emits no sulfur, no mercury, and much less nitrogen oxides (NO_X) and carbon dioxide (CO_2) than the competition. But, with the partial exception of sulfur (for which allowance programs exist under the acid rain law), this superior environmental performance has no economic value in the market place. The financier wants to know whether the plant will be able to run more cheaply than the competition. If the competition is a group of grandfathered coal-fired powerplants, the answer often will be no and the new plant may not be financed.

To address the egregious health, environmental, and economic flaws in the current air pollution control programs a number of bills have been introduced in Congress. Notable examples include Congressman Pallone's "Fair Energy Competition Act of 1999" (H.R. 2569), and the Waxman-Boehlert "Clean Smokestacks Act" (H.R. 2900). These bills establish industry-wide caps on tons of each of the "four-horsemen" pollutants: sulfur dioxide (SO_X), NO_X, CO_2, and mercury. The caps on SO_X and NO_X would provide building blocks for meeting health-based smog and fine particle standards and would reduce acid rain further. The mercury cap would attack the largest single remaining U.S. source of this pollutant. And the CO_2 cap would return emissions to 1990 levels—the target set in the 1992 Rio Climate Treaty that the U.S. has ratified.

With the exception of mercury, for which there are both local and regional concerns, these bills would implement the cap through a marketable permit program where power generators could trade their clean-up obligations to meet the caps in the most efficient manner. A "generation performance standard" would create a level playing field for generators—the standard would define the amount of pollution that could be legally emitted for a kilowatt-hour of electricity. This system will directly reward cleaner, more efficient generators.

In contrast to the current situation, if these bills were law, a developer of a new clean powerplant would be able to show direct tangible economic benefits from its reduced environmental impact. Because the new plant would be able to generate electricity below the law's "generation performance standards," for every kilowatt-hour sold, the plant would produce another profit-making product: emission allowances that can be banked or sold on the market. This additional revenue stream would make financing such projects that much more attractive.

A final benefit of these integrated pollution cleanup bills is that they provide a clear roadmap for business in planning long-term investments. The history of clean air progress has developed as a series of unconnected initiatives, typically focused on a single pollutant. Today we can survey the next 10-15 years and be confident that additional measures will be pursued to reduce the four horsemen pollutants.

But if we pursue the traditional approach, no one can say now with confidence, when, how deep, and in what order these important steps will occur.

As a result business planners must approach today's investments by making educated guesses about environmental requirements. Billions of dollars are changing hands as generation plants are sold under state restructuring programs. One thing we can say for sure is that someone is guessing wrong. By enacting integrated cleanup programs Congress could both provide certainty and reduce the tendency to prolong dependence on existing outmoded plants through the traditional process of applying end-of-pipe cleanup devices normally aimed at controlling only one pollutant.

In short, we know we need to reduce a range of damaging pollutants from the electric generating sector; we know how to do it; and we know that failure to take these steps as part of restructuring legislation will increase damage, prolong uncertainty, and encourge unfair competition. Mr. Chairman, your committee has jurisdiction over both the economic and environmental performance of this industry. We urge you and your colleagues to avoid an arbitrary separation of these interdependent issues. Instead we hope you will seize the opportunity to demonstrate that Congress can address the key issues that face the industry and the public in a manner that produces a cleaner, more efficient, more sustainable, and more competitive industry that delivers energy services for lower costs.

Mr. BARTON. Thank you very much.

Next we will hear from the final member of this panel, Mr. Rao, president of Indiana Municipal Power Agency.

Welcome. Your full testimony has been submitted for the record, if you would summarize. You have 6 minutes.

STATEMENT OF RAJESHWAR RAO

Mr. RAO. Thank you, Mr. Chairman and members of the committee.

My name is Rajeshwar Rao. I am the president of the Indiana Municipal Power Agency.

IMPA is a political subdivision of the State of Indiana, created in 1980 to allow its 31 municipal members serving 250,000 people to jointly finance, develop, own, and operate electric generation, transmission, and local facilities in Indiana.

We are relatively unique because we own $50 million worth of transmission facilities that make us jointly own Cinergy's transmission grid, and also obtain transmission from others to meet the needs of our members.

I am here today to testify on behalf of the Transmission Access Policy Study Group. TAPS is an informal association of transmission-dependent utilities in 29 States created to promote open, equal, nondiscriminatory access to the Nation's electric transmission grid.

IMPA and other TAPS members have been buying and selling electricity in wholesale markets for more than 20 years. We know from first-hand experience that merely declaring that there should be competition and open access does not make it so.

After decades of operating particularly integrated monopolies, the industry will not magically transform into one characterized by vigorous competition without decisive action from Congress to restructure the industry for competition.

TAPS believes that Federal restructuring legislation is needed to make retail competition work for consumers. However, if we are serious about electric competition, it is absolutely critical that we get the basic structure right and provide the tools needed to ensure that Federal legislation achieves its promise of true and fair competition in the electric power marketplace. Only then we can en-

sure that restructuring will lead to lower prices for all consumers across the Nation.

Basic concerns about how H.R. 2944 fails to meet and fully address transmission market power are covered in my written statement, and in the oral statement of APPA and CFC, also. But I want to use my time to answer important questions which were asked yesterday.

There are several questions I can answer with real-life examples. I will try to cover some of them in my 5 minutes, but would like to share the other examples later if time permits.

Question one: are RTOs needed? Absolutely. You will not get competition without it. For example, TAPS members, Oklahoma Municipal Power Authority, have been trying to purchase 15 megawatts from Duke Energy Trading and Marketing for the summer of 2000. Although Duke requested transmission from a competitor nearly a year ago, the competitor has refused to answer, stating only that transmission of this small amount of power is under study.

There is no way to know if this is a stall because there really is not a mere 15 megawatts of transmission capacity available, or, on such a huge system, whether they are improperly holding the capacity. We do not know.

Under these circumstances, it is not surprising in this situation, where transmission limitations preclude access, OMPA received only seven responses, most of which were transmission contingent to its recent RFP which it sent to 100 suppliers. With an RTO, the transmission decisions that are critical to competition would be made by the independent RTO, assuring they will be non-biased. Rather than re-regulation, RTOs are an essential step toward the more lightened FERC regulation.

Next question: will voluntary RTOs work? No. Transmission owners will not voluntarily relinquish their current ability to use their ownership and control of transmission to prefer their own generation. For example, TAPS member Florida Municipal Power Agency has worked hard to get most of the market participants in the State, including the co-ops, power marketers, the developers of big power, utility and board to support creation of some form of RTO. However, these efforts are currently at stalemate by the opposition of the two largest utilities, who control 90 percent of the transmission in the State.

If utilities can join and shape their own RTOs, will that work? No. To do their job in promoting competition, RTOs must be large and rationally configured, not configured to increase the market power of participating utilities.

For example, I have a picture here showing the midwest and connecting to the east coast. AEP, back in the map, is located in the Ohio/Indiana/Virginia area. They tried to negotiate participation in the midwest ISO, the blue section, but after some time, after about a year, they said that they would rather form their own Alliance RTO and created a barrier.

I want to give you some examples of how AEP's transmission is a barrier to Cinergy. BOTH AEP and Cinergy have generation located in the Ohio valley where there is surplus power.

It is cheaper to transmit electricity to the white section, but, on the other hand, by creating a barrier, AEP differentiated the generation facilities owned by Cinergy and AEP, making Cinergy generation facilities more expensive than AEP generation facilities.

Since the red light is on, I am going to stop here, but I have several true, real-life examples of market power in both generation and transmission. I will respond to questions later.

Thank you, Mr. Chairman.

[The prepared statement of Rajeshwar Rao follows:]

PREPARED STATEMENT OF RAJESHWAR RAO, PRESIDENT, INDIANA MUNICIPAL POWER AGENCY ON BEHALF OF TRANSMISSION ACCESS POLICY STUDY GROUP

Good morning, Mr. Chairman and Members of the Subcommittee. My name is Rajeshwar Rao. I am President of the Indiana Municipal Power Agency (IMPA). IMPA is a political subdivision of the state of Indiana created in 1980 to allow its 31 municipal members to jointly finance, develop, own and operate electric generation, transmission, and local facilities to provide for their electricity needs. IMPA's 31 member municipalities currently serve approximately 250,000 people.

IMPA is relatively unique because we are both a transmission owner and a transmission dependent utility. IMPA has invested some $50 million in transmission facilities that are part of a Joint Transmission System in Indiana, through which we have rights over the entire Cinergy transmission system. At the same time, IMPA is a transmission dependent utility with respect to access for our member municipal systems connected to the AEP transmission grid, and access to our ownership share of a Louisville Gas & Electric generation facility in Kentucky.

Because of this dual role, IMPA is keenly sensitive to the importance of establishing a transmission system that is open, fair and non-discriminatory. As a result, we have been aggressive advocates of establishing fully independent Regional Transmission Organizations (RTOs) that are fair to both transmission owners and transmission users. Nothing short of a totally "color blind" RTO that treats all transmission owners and users the same, regardless of who owns particular transmission facilities, will succeed in achieving Congress's goal of establishing a truly competitive market place for electricity.

I am here today to testify on behalf of the Transmission Access Policy Study Group (TAPS). TAPS is an informal association of transmission dependent utilities and other supporters in 29 states created to promote open, equal, non-discriminatory access to the nation's transmission grids. IMPA, like the other municipal, cooperative and investor-owned utilities, and municipal joint action agencies that are members of TAPS, must depend on the use of transmission systems of large vertically-integrated utilities in order to reach alternative sources of power supply for our consumers. TAPS members have been active in wholesale markets for some 20 years, and have been on the "bleeding edge" of efforts to obtain transmission service, open access, and RTOs. We know from first hand experience that, given the crucial role of transmission and the current industry structure, merely declaring there to be choice will not magically transform the electric industry to one where the price of generation is determined by the invisible hand of vigorous competition.

TAPS has concluded that the only way to get to a competitive electricity industry is by restructuring the industry to provide the transmission and market structure needed to allow competitive forces to work. We believe federal legislation is needed to achieve this critical objective, but it must be the right legislation. If the Chairman and the Subcommittee are serious about electricity competition, we need to work together to get the basic structure right, and to provide tools to ensure that the intended transformation stays on course. Watered-down or halfway measures simply won't work. Compromise on the key issues of industry structure will do far more harm than good.

The proposed Electric Competition and Reliability Bill, H.R. 2944, describes its purpose as "benefit[ting] American electric consumers through lower electric rates, higher quality services, and a more robust United States economy by encouraging retail and wholesale competition in electric markets . . ." TAPS shares the Chairman's goals. However, TAPS is concerned that H.R. 2944 will not achieve this purpose. Indeed, provisions of the bill appear likely to induce precisely the opposite effect: strengthening the grip of monopolists, and exposing consumers to electricity prices disciplined by neither the competitive market nor regulation.

Specifically, TAPS believes the bill fails to provide the transmission and market structure needed to support competitive wholesale and retail markets. We urge the

Subcommittee to amend H.R. 2944 to ensure that the bill serves its pro-competitive purposes.

With regard to transmission, the Subcommittee should:

1. Grant FERC the authority to require, without delay, participation in truly independent and rationally configured large, regional transmission organizations;
2. Prevent transmission owners from evading inclusion of facilities in RTOs by creative reclassification of high voltage transmission facilities to distribution; and
3. Place regulatory responsibility for transmission service clearly in FERC's hands.

With regard to generation market power, the Subcommittee should:

1. Empower FERC to take steps to remedy and prevent the exercise of market power and market manipulation; and
2. Eliminate or revise the proposed unworkable time limits on FERC merger review and clarify FERC's authority to review mergers involving generation-only facilities.

TRANSMISSION

1. FERC needs authority to require strong, independent, broad regional RTOs.

H.R. 2944 correctly recognizes that the current regimen of control of transmission by individual vertically-integrated utilities must change to be compatible with competition, and that a regional transmission organization is the structure needed in a competitive electric industry. While TAPS applauds the Chairman for recognizing the need for RTOs, we are concerned that the proposed RTO provision is so compromised as to largely defeat the intended pro-competitive purposes.

• **Independence:** RTOs are critical to removing control of the transmission facilities, which all competitors need to use to reach the market, from the hands of one set of market participants that can use that control to favor themselves. Instead, control of transmission should be placed in the hands of a competitively neutral, independent body. The proposed legislation starts out by correctly recognizing that RTOs "must be independent of all market participants, and no market participants may exercise control over the operation of the [RTO]." However, it then compromises the "bedrock" RTO concept of independence by expressly defining it to ignore retention of 10% of the voting shares and unlimited non-voting "passive" interests that include rights to "participate in major corporate changes" to the RTO. Adoption of such lax standards means that the RTO will never be fully independent of market participants, leaving self-favoritism and undue discrimination a continuing and ever-present threat. In an RTO with 5 participating transmission owners, each of whom retained a 10% voting share, the transmission owners could hold a 50% voting interest. **Instead of legislating plainly non-independent RTOs, the Subcommittee should insist on RTOs that achieve a clean structural break, completely separating transmission control from generation interests.**

• **Scope/pancaking:** As FERC has recognized, RTOs can facilitate competition by ending the current system of balkanized markets, where an additional "pancaked" rate (or toll) must be paid whenever a transaction crosses the boundaries from one transmission owner to the next. In contrast, RTOs would permit competitors to sell their electricity goods throughout a broad regional market by payment of only a single "non-pancaked" charge. By expanding the market, RTOs can increase the number of buyers and sellers that can transact with each other, enhancing competition and reducing market power. H.R. 2944 threatens to undermine this critical RTO role by giving at least tacit approval to the concept of RTOs comprised of just a single utility, preventing FERC from requiring utilities to join an RTO other than the one they propose (unless the bill's standards are not met), and permitting pancaked rates to continue for a "transition" period. Given the delayed implementation of this provision, pancaked rates could well be in place during the critical first years and indeed decade of retail competition, or not eliminated at all in the case of single utility RTOs. Also lethal to competition are gerrymandered RTOs designed by a group of vertically integrated transmission owners to enhance their market power by creating barriers to competitors. H.R. 2944 seems to foster such anticompetitive RTOs, rather than give FERC clear authority to ensure that RTO boundaries are dictated by the scope of regional markets, not by individual company desires to protect the value of its generation or achieve a competitive advantage. **The Subcommittee should grant FERC express authority to require participation in RTOs that have a large regional scope designed to facilitate competition and enhanced reliability, and to eliminate pancaked rates. As noted by APPA, the statutory criteria will need to accommodate unique characterizations and legal arguments of public power.**

• **Authority to require construction/incentives:** The proposed legislation correctly acknowledges the RTO role in planning additions, but gives RTOs no role in

requiring construction of grid expansions. Instead, the legislation endorses the use of incentive rates to induce transmission owners to construct (as well as to join RTOs). Bribing transmission owners is neither a necessary nor an appropriate means to ensure the transmission infrastructure needed for competition. Indeed, the costs associated with such inducements not only needlessly saddle consumers with excessive costs, but undermine the competitive forces RTOs are intended to promote by paying one group of competitors monopoly rents for their transmission. The best way to induce construction is to fully separate transmission from generation interests, so decisions to expand are not influenced by how the expansion affects the value of the transmission owner's generation. Providing RTOs the authority to cause needed construction by the transmission owner or others opens the doors to market-based means to get the needed transmission constructed efficiently—by bidding out construction to third parties. **Instead of endorsing incentives, the Committee should strengthen the RTO's authority to require construction and enable FERC to evaluate the best means to ensure prompt construction of needed grid additions.**

• **Delayed implementation/incomplete remedies:** H.R. 2944 as proposed puts RTO formation on a slow track. Transmitting utilities need not join until January 1, 2003 and even that date may be postponed "pending any proceeding under this section or Section 313," the Federal Power Act's judicial review section. A recalcitrant transmission owner can postpone for years the date when it must finally join an RTO and relinquish its ability to use ownership and control of transmission to benefit its generation sales. In the meantime, it can use its potent power to choke off competitive retail markets in their infancy. The provision for "transitional" pancaked rates further removes from consumers the benefits RTOs are intended to provide. The RTO provision is also weakened by the absence of clarity on key points, such as what happens if a transmitting utility does not join an RTO, and what happens if FERC does not initially approve the proposed RTO or withdraws its approval. **Particularly given FERC's RTO Rulemaking, the legislation should require prompt formation of RTOs, and give FERC the tools to demand adherence to the provision.**

2. Provisions are needed to prevent transmission owners from evading inclusion of facilities in RTOs.

The proposed legislation sets forth a seven-factor test for distinguishing transmission from distribution facilities, and requires FERC to give maximum deference to a state's determination. This provision lends itself to abuse that could result in empty RTOs, thus gutting the interstate transmission infrastructure necessary to support vigorous wholesale and retail competition. RTOs will not provide the needed neutral infrastructure if transmission owners are allowed to create competitive barriers by restricting the facilities to be subject to RTOs. Given the regional nature of RTOs, equity demands that there be consistency from state to state, utility to utility, in defining the facilities subject to the RTO. Finally, removal of needed transmission facilities from RTO control by artificial reclassification will impede the RTO's ability to reliably and efficiently operate the grid.

TAPS members have seen "7-factor test" filings being made around the country as a means to escape FERC's open and non-discriminatory access requirements, and to retain effective control over transmission while ostensibly surrendering facilities to an RTO. In one such filing, Wisconsin Public Service Company sought to reclassify to distribution all but 124 miles of its nearly 1500 miles of high voltage transmission lines now subject to FERC open access tariffs, leaving only 7 of its 33 interconnections with other utilities subject to FERC transmission regulation. Although that filing was withdrawn in response to political pressure, others have followed the same tactic. For example, Commonwealth Edison has refunctionalized 40% of its formerly transmission facilities (including 345 kV facilities) to distribution.

TAPS submits that these evasion tactics, which threaten to undermine the effectiveness of the RTO provision, as well as FERC open and non-discriminatory access requirements, should be stopped. The bill should include a presumption, rebuttable by clear and convincing evidence, that non-radial lines in excess of 60 kV be classified as transmission. Such a standard would be consistent with my experience regarding the typical function of non-radial facilities of such voltage.

2. FERC must be responsible for regulating interstate transmission.

For electricity competition to be successful, it is essential that FERC have authority to establish one set of rules for the use and operation of the nation's interstate transmission system. The Eighth Circuit, however, recently undermined FERC's ability to do so. The court ruled that states can set their own rules for the transmission of "bundled" retail sales (traditional retail sales where the price for power

is "bundled" with the price of transmission and distribution services) and favor these in-state users when there is insufficient transmission capacity. *Northern States Power v. FERC,* 176 F.3d. 1090 (8th Cir. 1999).

Under *NSP*, each state can set its own rules for transmission of bundled retail sales within that state, without regard to what other states do and without regard to FERC's rules, while FERC is limited to setting rules for wholesale and "unbundled" (choice) retail uses. No regulatory body would have authority to ensure a coherent scheme for the use and allocation, among all users, of what is necessarily the single transmission network.

Think what pandemonium would occur if the interstate highways posted two sets of speed limits, one for in-state cars and the other for cars going out of state. Think how many crashes would occur if the state established a different regime for preferred in-state cars to switch lanes—they need not look or signal, because they are to be accorded priority. Imagine further that a state could establish a rule that if there was congestion, in-state cars would be permitted to pass, while out-of-staters would have to wait on the side of the road until the traffic subsided. Interstate commerce would plainly be impaired.

As we move toward competition on a state-by-state basis, it is essential that FERC be authorized to establish a single scheme for use of the grid that does not relegate use of the grid for wholesale sales or retail choice programs to second class citizen status. Consumers will not switch suppliers if they cannot rely on obtaining power. The absence of a clear, unified set of rules would also enable one state to cripple choice programs in a neighboring state, by according in-state bundled sales a higher priority than unbundled deliveries to its neighbors.

TAPS believes NSP to be wrongly decided under the current Federal Power Act, which provides FERC authority, without limitation, over transmission in interstate commerce. (We understand that FERC is considering seeking Supreme Court review.) The proposed bill, however, defines FERC jurisdiction as encompassing wholesale and unbundled retail transmission, while carving out expanded state authority over transmission of bundled retail sales. In this way, the proposed bill legislates at best confusion, and at worst NSP's absurd and counterproductive result. TAPS urges that the bill recognize that there can be only one set of rules for all users of the interstate transmission network, and those rules need to be set by FERC.

GENERATION MARKET POWER

1. FERC should be empowered to take steps to remedy and prevent the exercise of market power and market manipulation.

The structure and physics of the electric industry make it extremely challenging to transform into a robustly competitive industry, where market forces rather than regulation set generation prices. Not only do today's vertically-integrated monopolists have the ability to use their vertical market power derived from owning and controlling the transmission highways to foreclose others from competing to economically and reliably serve their load, but ownership of generation tends to be highly concentrated within geographic markets. Electricity is an enormously complex networked industry, in which operation of generation affects transmission availability for competitors and electricity must be produced at the same time as customers need it because it typically cannot be stored. These characteristics create many hidden opportunities to manipulate and control the market. Large incumbent utilities, which dominate various markets as a result of their history as state sanctioned monopolists, are in a position to effectively foreclose competition.

Getting to real competition in a highly monopolistic industry with the complexities of electricity supply is a major undertaking. In the long run, properly structured, truly independent, large regional RTOs, which have the authority to plan and implement necessary grid additions, can go a long way toward mitigating market power concerns by expanding the market and eliminating constraints. However, elimination of constraints will not happen overnight, or necessarily even in the first decade after effective RTOs are up and running. Either due to the existence of transmission constraints and natural geographic barriers, or due to the existence of artificial barriers and walls created by vertically-integrated organizations, generation market power does exist within geographic regions of the country and will continue to exist, even with RTOs. FERC needs the authority to identify and impose adequate remedies to correct such market power problems if there is to be effective competition.

Thus, to ensure the competitive infrastructure needed for competition to flourish, Congress will need to transform FERC from a price-setting agency to one with clear and specific responsibility to ensure that interstate markets for electricity are and

remain vigorously competitive for the benefit of all consumers. FERC needs explicit authority to take whatever actions are necessary to remedy generation market power problems that threaten emerging competitive markets, particularly in the likely-to-be-lengthy transition period. This authority must include a variety of tools that FERC can employ where necessary, including requiring the auction of capacity for periods of at least four years; cost-based rates; public disclosure of information (including transparent pricing); shared access to assets or services on a nondiscriminatory basis at reasonable rates; or, where other measures prove insufficient, divestiture of assets for fair value. Unfortunately, H.R. 2944 makes no effort to address this critical structural issue.

Because of the interstate nature of the grid and emerging markets, individual states will be powerless to effectively address this problem. Given the technical complexity of the industry and its real time nature, this task will be best accomplished by empowering FERC to meet its new responsibilities rather than relying on slow and expensive antitrust litigation, at least through the transition to mature competitive markets. Indeed, the Department of Justice and the Federal Trade Commission have conceded that antitrust laws alone are not adequate to address pre-existing market power. Above and beyond FERC's RTO and merger authority, the Subcommittee should grant FERC new authority to move quickly and decisively to eliminate undue generation market power as it arises, and to impose stiff penalties for market manipulation, in order to make such manipulation a very risky venture.

2. The proposed unworkable time limits on FERC merger review should be revised and FERC's authority to review mergers involving generation facilities should be clarified.

TAPS applauds the Chairman for maintaining FERC authority to review mergers, and abandoning the approach taken in the draft bill of stripping that critical authority from FERC. Given the potential for mergers to increase market concentration and restrict competition at the time FERC and the Congress are attempting to promote wholesale and retail competition, preserving this important function is vital.

TAPS is concerned, however, that the time limits proposed to be placed on FERC review will nevertheless de facto deprive the public of effective FERC review of mergers. Unlike the Department of Justice and the Federal Trade Commission, FERC operates without the benefit of the powerful Hart-Scott-Rodino information tools. In addition, FERC review is an open process, involving the public who can provide real world experience that can assist in evaluating the merger. Granting FERC merger authority, while depriving it of the time to gather and analyze the information needed to meaningfully assess the likely impact of the merger on competition, is a bad compromise that threatens to undermine the competitive industry structure the bill is intended to promote. Indeed, the time limits may well encourage merger applicants to be slow to provide the Commission (much less intervenors) with the essential information, cloaking it with claims of confidentiality and the like.

TAPS recognizes that the Subcommittee may be concerned that the current system creates the potential for effective denial of mergers by delay. The answer, however, is not establishing unworkable time limits that negate FERC review of mergers with significant competitive consequences. Rather, an alternative approach needs to be developed that affords FERC the opportunity to do its job well, while respecting the reasonable needs of merger applicants. For example, the legislation could require FERC to expedite approval of non-controversial mergers, and could provide procedures, including information requirements for applicants, which will help expedite the more difficult to analyze mergers.

In addition, TAPS recommends that the Subcommittee clarify FERC's jurisdiction over mergers of generation-only companies, to ensure FERC review of all mergers and acquisitions that can affect the structure of the electric industry. The absence of such clarification invites evasion of FERC authority.

TAPS appreciates this opportunity to present its views on H.R. 2944 to the Subcommittee.

Mr. BARTON. Thank you, Mr. Rao.

I will now recognize myself for 5 minutes, and maybe longer. And let me just say, as many of you have testified before and been here, it is good for us to continue to move on. Most members have the statements, so if some members missed your testimony, they will get back for the opening comments, or at least for the questions, but it is, I think, better for all of us as we keep moving on in the hearing so that we can get to the second panel eventually.

Let me start.

You know, I have heard from the Illinois Municipal Electric Agency that generation market power, horizontal market power, will be a problem in a deregulated electric industry. Some of you have testified to that.

There are no market power provisions in H.R. 2944 other than RTOs, because the hearing record seems to have made it clear that they are not necessary, based upon our previous hearings.

When I asked the DOE witness yesterday about this issue, he could not explain the problem.

Mr. Rao, in your written testimony, it also does not explain the problem, although I think maybe you touched on it in some of your questions and probably will have more real-life examples to share, and so there is a frustration evident in my search for an answer.

Some people say there is a problem, but there is a refusal to explain technically how it becomes a problem, so I would like to ask this question to Mr. Rao and Mr. Owens, to explain the problem clearly and directly for the subcommittee and answer these questions directly.

Exactly why cannot RTOs mitigate horizontal market power? And are there circumstances where generation market power exists today?

Mr. Rao, why don't we begin with you?

Mr. RAO. I have an example for the second part of the question, and then I will go back to the first part of the question.

Generation market power is the ability of one or a few utilities to increase the price above the level that would apply in a competitive market with many competitors.

The combination of high concentration levels resulting from development of this industry and State-sanctioned monopolies coupled with transmission limitations creates the situation where, in many places in the country, there is clear market power, and utilities are willing to take steps to keep it that way.

To give you an example, Florida is a peninsula with high growth load coming into the State. There is about 38,000 megawatts of load at present in Florida, and only 3,600 megawatts of limited import capability, and there are two major utilities that own about 75 percent of generation to meet that load.

Recently, one of the subsidiaries of Duke Energy, wanted to build a merchant plant in Florida with about a mere 500 megawatt capacity. They wanted to build in one of the municipalities which is a member of TAPS.

When Duke Energy's subsidiary asked the public service commission for approval, the two investor-owned utilities with the 75 percent generation market power intervened to stop that project, and when they did not succeed, when the commission approved that particular proposal, they even took it to the Florida Supreme Court. It is right now pending.

It says that the utilities with existing market power will try to stop new entrants.

Mr. BARTON. That is an example. Of course, we all know that Florida is almost, for some aspects, almost not considered part of the continental United States because it is a peninsula. So how about inside the mostly contiguous 47 other States?

I am in trouble. I am not going to run nationwide, I will tell you that.

Mr. RAO. I do have another example which exists within the—not necessarily Florida.

Mr. BARTON. Could you briefly, because I want to get Mr. Owens' answer to this question, also.

Mr. RAO. Yes.

Mr. BARTON. Just give me the location and the company.

Mr. RAO. Eastern Wisconsin has the same type of situation with a 10,000 megawatts of load and 1,200 to 1,300 megawatts import capacity, almost all of which is controlled by three major utilities in eastern Wisconsin.

These three utilities together control more than 90 percent of generating capacity——

Mr. BARTON. But there are three utilities that have competition in that market, or would have?

Mr. RAO. They are——

Mr. BARTON. I mean, you are talking about three different producers.

Mr. RAO. Three different producers.

Mr. BARTON. Let me move to Mr. Owens. I have got the ranking member here bugging me to move along.

Mr. Owens?

Mr. OWENS. You asked the question whether regional transmission organizations would help mitigate market power, and I would say yes, they would.

The issue of market power, if I might just break it down into two components, first, one area relates to what we call "vertical market power," and historically that has related to your access to the transmission system.

All investor-owned utilities are required by law to provide nondiscriminatory access to the transmission system under FERC's implementing Order 888. Certainly regional transmission organizations would seek to make sure that access to the grid is proper.

In addition, you asked a question relating to horizontal market power. Horizontal market power, many folks generally relate that to your ability to control the generation market.

As I indicated in my oral remarks and in the written statement that I provided for the record, there is an explosion of participants in the bulk power supply market. There are no barriers to entry to that market. We have thousands of independent power producers.

As others have indicated, there is a significant opportunity for generators to locate in all aspects of this market, so I do not believe that there is the existence of horizontal market power.

Now, to the degree that there is, the States are well equipped to deal with those issues. I do not believe that there is a need for additional Federal authority to deal with the issue of horizontal market power.

Mr. BARTON. Thank you, Mr. Owens.

I would like to turn now and recognize for 5 minutes the ranking member of the subcommittee, Mr. Hall.

Mr. HALL. Thank you, Mr. Chairman.

I am not pushing you, but I do have an 8 dinner meeting.

And, Ms. Church, I will give you some wisdom from the 1930's. Will Rogers said the way to solve the highway traffic problem was to require all automobiles to be paid for before they could get on the highway.

So you can imagine how bad it is now. I wish he could see it today. Will Rogers would not like anybody, would he?

I am not confused. I guess I am still confused, but I am trying to listen to this panel and glean from what you say what you mean and what you want.

I have heard Mr. Helton say we will be developing the proper amendments, and Mr. Nevius said we need reliability legislation now, and I do not know whether this requires some amendments or not. Ms. Church said the bill subjects certain aspects to intrusive State control. Mr. Owens said we have some concerns and objections, repeal PUHCA and reform PURPA and the bill repeals both. Mr. Mayben said the bill fails to treat all parties alike. Mr. English—I had to leave before I got to listen. I tried to listen to all of his, but I sure did not want to miss an important vote over there. But we urge the chairman to work on language.

How many of you are for the bill just like it is? How many of you are for the bill with a few amendments, not to completely restore the automobile, but just—1, 2, 3, 4, 5, 6. I count 12.

Well, let me see. Mr. Helton, let me ask you some questions here, if I might.

Your statement says H.R. 2944 is not a perfect bill but a good one, right?

Mr. HELTON. That is correct.

Mr. HALL. And your testimony lingers long on the merits of the legislation. Let me ask you about some of the problems that you have with this legislation and, if you can—and maybe you cannot—give me a yes or no answer, or tell me you cannot answer it.

On TVA, the bill preserves TVA consumers first call on cheap power, permits TVA to build a new generation of facilities, and allows TVA to sell outside the valley. Do you support that or not?

Mr. HELTON. Do not.

Mr. HALL. And Bonneville, the bill would permit Bonneville to recover its stranded costs through a surcharge on transmission consumers that would raise costs for other users, such as California consumers who use the system for retail purchases. Do you favor that as written?

Mr. HELTON. Under reasonable terms, probably yes.

Mr. HALL. You would have to have an amendment there though?

Mr. HELTON. Yes.

Mr. HALL. State preemption—the bill imposes a Federal hard reciprocity provisions. This would reduce the number of suppliers from whom the consumers in open States could purchase and preempt State laws to the contrary. Do you support that?

Mr. HELTON. We would like to amend that one, as well.

Mr. HALL. Okay. That is one you do not like and two to amend.

Do you support the provision on RTO mandates? The bill includes a Federal mandate requiring transmission owners to join a regional transmission group by the year 2003 and setting specific criteria for FERC appeal. Do you support that?

Mr. HELTON. Generally, yes. The specific criteria is the area of concern.

Mr. HALL. Okay. You cannot give me a yes or no on that?

Mr. HELTON. Cannot.

Mr. HALL. FERC merger authority—the bill expands FERC's merger authority to include transmissions involving generation facilities and holding companies. Do you support that as written?

Mr. HELTON. Yes.

Mr. HALL. That is the first unequivocal yes, is it not?

Mr. HELTON. No, sir. I think—didn't I do that on the first one?

Mr. HALL. You may have. Yes.

Mandatory interconnection to local distribution systems—this bill gives distributed generators of a considerable size, up to 50 megawatts, the right to interconnect with local distribution companies. Do you support that?

Mr. HELTON. No.

Mr. HALL. And then, let me see, your statement indicates that your coalition will be developing perfecting language. Do you have a time on when you are going to submit that language and you are going to give it to the chairman? He has been very open with us, and he will immediately send it on to us. Do you have those amendments ready?

Mr. HELTON. Almost.

Mr. HALL. Okay. I think my time is up. I have two more pages of questions here, but I will get back to you maybe. Thank you.

Mr. BARTON. As long as we do not run past 8, we are going to be fine with Mr. Hall.

I will now turn to my colleague from Kentucky, Mr. Whitfield, for 5 minutes worth of questions.

Mr. WHITFIELD. Thank you very much.

Mr. English, in your testimony you focused on some of the major concerns of the co-ops, and I noticed that in your testimony you also talked about some concerns about section 103 of the bill relating to the regional transmission organizations, and I was just wondering if you could elaborate on that a little bit more?

Mr. ENGLISH. Mr. Whitfield, our association strongly supports voluntary RTOs. We do feel that that is an important element. We are also concerned, I might say, about the fact that RTOs are regulated by the Federal Energy Regulatory Commission, and, as far as members of RTOs, that seems to be the appropriate way for us to address that, particularly as you are dealing with some of the smaller entities such as electric cooperatives.

We think that the RTO provision that is contained in the bill, which also allows for members to set up their own RTOs, is one that has some promise. We would like to do some work and, I suppose, like the other members here on the panel, we probably have got some ideas in mind for amendments. But that is the position that we take on RTOs.

Mr. WHITFIELD. Okay. And then I had not heard a lot of discussion about this net metering issue. Could you elaborate on that just a little bit?

Mr. ENGLISH. Well, as far as any net metering, it has to do with those who also may be—consumers who may be generating some

power on their own and may be able to sell it back through the grid.

The issue, I guess, is what is the net between the two.

Mr. WHITFIELD. Right.

Mr. ENGLISH. That, as I understand it, while it may sound good on paper, may have some real difficulties in the real world as you attempt to integrate that into the process and the grid, itself.

Mr. WHITFIELD. Okay. All right. Thank you.

Now, Mr. Hawkins, yesterday, when the Administration testified, and then when Secretary Richardson had testified on this previously, and even Carol Browner testified, they all sort of took the position that this restructuring legislation was not the right place or the right format to get into additional environmental legislation, and particularly on CO_2 reduction mandates and so forth.

That is still their position, but your organization obviously still feels that you want to pursue this; is that correct?

Mr. HAWKINS. Our organization and many other organizations believe that we should address the air pollution problem from this industry while we address its economic performance, and this is not the first instance that we have disagreed with the administration.

Mr. WHITFIELD. And will you all be supporting the Pallone-Waxman amendments in this area if they come forth with those, as they have discussed?

Mr. HAWKINS. Yes, sir.

Mr. WHITFIELD. Okay. Now, as you know, I represent an area that uses a lot of fossil fuel to generate its electricity, and one thing that is frequently referred to is that these coal-fired utility plants in the midwest and southeast are uncontrolled and that they are exempt from the Clean Air Act requirements, and yet all of these plants are required to comply with the national air ambient quality standards. All of them are required, under the Clean Air Act, to reduce their sulfur dioxide emissions by 50 percent below the 1985-1987 levels. The 1990 amendments also require these plants to reduce their nitrogen oxide emissions by approximately 40 percent below existing levels, and they would also be subject to any reductions on the EPA's proposed fine particle and 8-hour ozone standards. I know that there is a problem with that in the courts right now. But they do meet a lot of environmental standards and are required to do so. So would you elaborate a little bit on the concern that you have about these plants?

Mr. HAWKINS. Yes, sir.

The State of the law is that plants that were in operation before 1970 are treated fundamentally differently than plants that have been built in the last 30 years and plants that will be built tomorrow.

Modern plants are required to generate electricity meeting state-of-the-art performance standards in terms of how clean you can generate electricity. Older plants are not required to do that. Older plants are allowed to rely on a patchwork of regulations that differ from State to State, and, as a result, the facts are clear: the power produced from an older plant pollutes sometimes 3, 4, 5 times as much as a competitor's power from a modern plant.

We think that that is an outmoded policy and one that is still causing a lot of environmental harm.

Mr. WHITFIELD. But you do not deny that they are meeting the legal requirements that they must meet today?

Mr. HAWKINS. Well, the trade press and some of the daily press have been filled with reports in the last several months about inquiries as to whether, in fact, some of these plants are complying with their legal obligations; specifically, whether they are complying with their obligations to seek a permit when they make certain major changes in the operations or the physical aspects of their facilities.

We are aware that the New York attorney general has sent notice letters stating his conclusion that a number of these companies are, in fact, violating the law, and we have read trade press reports that the USEPA is carrying on its own investigation.

So no, sir, we do not think it is clear that they are meeting all legal obligations.

Mr. WHITFIELD. But even if they are, you still would like to see the law changed as it relates to them?

Mr. HAWKINS. That is correct.

Mr. BARTON. The gentleman's time has expired.

The Chair recognizes the gentleman from Ohio, Mr. Sawyer, for 5 minutes.

Mr. SAWYER. Thank you, Mr. Chairman, and thanks to our entire panel.

Let me turn first to Mr. Nevius. First of all, thank you very much for all of the work that NERC has done. It has been important and central to a lot of the legislation that we have.

I am assuming that you fully subscribe to the notion that electric supply could deteriorate over the long term if transmission capacity does not keep pace with growth and demand?

Mr. NEVIUS. The reliability of the electric grids could certainly be at risk if we do not have a way to enforce mandatory standards. The issue of electric supply involves other things in addition to the amount of transmission, including the amount of generation and what kind of demand side measures of programs.

Mr. SAWYER. Of course. But transmission——

Mr. NEVIUS. But transmission——

Mr. SAWYER. [continuing] adequacy is in strength, no matter how much generation exists, if it is not adequate? You would agree with that, I am sure?

Mr. NEVIUS. Yes.

Mr. SAWYER. The amount of transmission that is planned for the next few years, however, is substantially less than we talked about even a few years ago. Am I correct in that?

Mr. NEVIUS. The amount that has been planned to be added has continued to decline over the last 10 to 15 years.

Mr. SAWYER. Let me ask you, with regard to NERC's comments on the RTO, NERC asserted that transmission rates must provide incentives to get the right amount of transmission infrastructure built. Do you agree with NERC that we must ensure that enough transmission capacity is available to prevent short-circuiting competition?

Mr. NEVIUS. I guess the comments that we made regarding RTOs and also the adequacy of transmission indicate that various proposals to provide incentives in one form or another are certainly not inconsistent or incompatible with the self-regulatory reliability concept that is contained in title II, and we are not proposing specific pricing or incentive mechanisms, themselves.

Mr. SAWYER. I understand that, but it is your assertion that incentives are useful and necessary?

Mr. NEVIUS. They can be. Yes.

Mr. SAWYER. Yes. Thank you very much.

Ms. Church, I understood yesterday that the deputy secretary of Energy said that incentives are not necessary to attract transmission investment. Do you agree with that?

Ms. CHURCH. We agree. We believe that in some cases incentives may be appropriate. We think the whole system really needs to be re-looked at, because it was developed for a system that is changing substantially.

Mr. SAWYER. For very different purposes.

Ms. CHURCH. Yes.

Mr. SAWYER. Yes. I agree.

Can you speak to your notion of what incentives might be useful, helpful, necessary?

Ms. CHURCH. I would be glad to provide the member with some comments to elaborate on that.

Mr. SAWYER. That would be great. Thank you.

Ms. CHURCH. Thank you.

Mr. SAWYER. I am assuming, from what you have said, then, that you would agree that if more robust transmission networks do not develop, that the whole notion of how we go about achieving the level of competition we are trying to achieve simply cannot take place?

Ms. CHURCH. Well, I believe it can be ameliorated by the development of RTOs. For example, one of the things that we have seen over the last several summers are curtailments of large amounts of power that have a cascading effect on the rest of a whole region, and the example I used in my testimony was the Michigan/Ontario incident.

Mr. SAWYER. Sure.

Ms. CHURCH. If the midwest had a large RTO, it would have helped to internalize those constraints, and it may have prevented the curtailment of 400 megawatts.

Mr. SAWYER. The real problem there was high delivered prices and not necessarily high generated prices.

Ms. CHURCH. But the whole reason was that power was unable to move into that area. In curtailing to alleviate a 400 megawatt constraint, 4,000 megawatts were actually curtailed, which kept power from coming in from New York and PJM into the midwest, which created a shortage of generation, which, of course, drove the prices up.

We believe we do need new transmission, but the existence of good RTOs would alleviate a lot of the problems that we are seeing.

Mr. SAWYER. Thank you very much. I see my time has run out.

Mr. SHIMKUS [presiding]. Thank you. Your time has run out. Thank you very much.

Now I will recognize the gentleman from Oklahoma, Mr. Largent, for 5 minutes.

Mr. LARGENT. Thank you, Mr. Chairman.

Mr. Richardson, I would like to ask you, one of the things you talked about was the independence of RTOs. Is it your opinion that the ISOs that are currently in existence are independent?

Mr. RICHARDSON. Ones that are in existence, ones that are being proposed are not—you cannot give a yes or no answer to that because each has different characteristics. Some are, some are not.

Mr. LARGENT. Okay. Let me ask you a question about market power. Can you talk to us a little bit about market power? I will give you my opinion here—market power exists because of physical realities of where generation is located, talking about horizontal market power, and physical constraints that exist because of the transmission lines that currently exist.

Talk to us about the transient nature of market power, in your opinion.

Mr. RICHARDSON. Thank you for asking that question.

Mr. Shimkus, if the record is incomplete with respect to market power, then that is our fault that we have not provided sufficient examples.

I would point, as examples, to the preamble of the regional transmission organization preamble from the Federal Energy Regulatory Commission, where they say open access is insufficient, the need for independent system operators is clearly demonstrated, and then they go on to give actual examples of abuses of market power where there are clear findings of problems in the abuse of market power by vertically integrated utilities where they favor their own generation because they control transmission. They give examples of situations where there have been allegations of abuses of market power. They note that in some cases individual companies—my members and others—are afraid to come forward for fear of retribution. So they suggest that perhaps we are seeing only the tip of the iceberg of the abuses of market power.

It is a marvelous piece of information. I hesitate to overburden this committee with further paper, because I have already done a pretty good job of that in my prepared testimony, but it is a very good piece that I think demonstrates the problems of market power and the remedies that are needed.

Now, when we are looking at market power, we have what I regard as institutional market power problems that arise from the vertical integration of our utility industry historically.

Regional transmission organizations, if they are properly structured and have the right boundaries that do not game the system by creating, rather than eliminating, constraints between high-and low-cost systems are the solution, and we need to move forward with those, and we should do so first in a collaborative fashion.

We strongly believe that the Commission in the end may need the authority to order utilities to participate in such organizations because that may be the only way to rationalize and get rid of the vertical market power that currently exists.

Horizontal market power, as I said in my opening statement, the ability to use vast amounts of generation to affect prices for consumers, not—because generation affects the way the transmission

system works, and so, by constraining generation by unscheduled outages of generation facilities can have economic consequences in the marketplace that need to be addressed, but I think this is probably a transitional issue. It is not necessarily one where FERC needs authority that exists in perpetuity, as I suggested in my oral statement. Perhaps what FERC needs is a tool box of remedies up to and including the dreaded "D" word, that being a divesture of capacity through a capacity auction for a period of time until these problems are addressed.

Other tools can be used, up to the point where they can come back and report to the Congress that the industry has been restructured, and that is really what we are talking about. We are talking about the structure of the industry, and that is why independent system operators are so critically important.

It is the structure that we have to get right. The Holding Company Act structured our industry for 60 years. now we are talking about taking that down. We are looking at a new structure, and this is an opportunity for this Congress truly to get the structure right.

These opportunities do not come along very often. That is why we want legislation now. We see the industry restructuring itself and we are concerned that the monopolists are controlling the restructuring of the industry, not policymakers who are looking out for the interests of the public.

I hope that—I got a little bit on my soap box, sir.

Mr. LARGENT. That is okay.

Mr. RICHARDSON. But I hope I addressed the question.

Mr. LARGENT. Mr. English, I want to give you a chance to address the issue of propane.

In what way does the Federal Government place limits on co-ops today in terms of their ability to expand their business opportunities? What is the mission of a rural electric co-op?

Mr. ENGLISH. Well, I think the mission of electric cooperatives, whether they are in rural areas or any other area, is one of meeting the needs of the consumer members, the people who choose to come together and make their purchases through the entity of a cooperative.

Mr. LARGENT. Meeting what needs? Their electricity needs?

Mr. ENGLISH. Whatever needs they may have.

Mr. LARGENT. Any need?

Mr. ENGLISH. Exactly.

Mr. LARGENT. Cable, DVS, propane——

Mr. ENGLISH. Exactly.

Mr. LARGENT. [continuing] groceries?

Mr. ENGLISH. As I used the example before this committee once before, to deny consumers the opportunity to do it for themselves, and that is basically what we are talking about, or do it as a group for themselves, is like denying someone to opportunity to grow tomatoes in their back yard garden and eat them. That is like saying you have got to sell them to the grocery store and buy them from the grocery store. You cannot eat your own tomatoes.

That is basically the same process that we are talking about here.

But as far as whether we are talking about propane or whether we are talking about any other service from the standpoint of an electric cooperative and recognizing the fact there are all kinds of different cooperatives—housing cooperatives, you have got farmer cooperatives, you have got a wide variety of different cooperatives in this Nation today—it also should be recognized, the fact that, for instance, under the Rural Utilities Service, any loans are specifically restricted only for electric utility service.

If they, in fact, use those funds for any other purpose other than for the infrastructure or assets of the electric utility, itself, they would be in violation of a loan agreement. Not only could they be declared ineligible for the loan, but they could also be declared—have the loan called at that particular time.

Mr. SHIMKUS. Has the gentleman answered your question?

Mr. BARTON. Well, we have Congressional courtesy. We let former Members speak a little bit longer than the other panelists.

Mr. SHIMKUS. Overruled by the chairman.

Just remember that, my friends on the left. I tried to get over there.

Mr. ENGLISH. In addition, I might add this also gets into the question of tax exemptions. Electric cooperatives are not for profit and are governed by the Internal Revenue Service. As such, should they, in fact, cross-subsidize, as some have argued, then they would be in violation of their—with the regulations of the Internal Revenue Service and could lose their tax-exempt status.

There are procedures for anyone who suspects that such violations are taking place to proceed, whether it be with the Rural Utilities Service or whether it be with the IRS.

And also, very quickly, let me say that any other businesses outside electric service, they would be subject to the unrelated business income tax, which is a Federal tax at the corporate level.

So there are taxes with regard to any of these other businesses, whether it be propane or whether it be anything else with regard to any margins that might result from that.

Those margins, by the way, could not go back to an electric cooperative as far as the rates are concerned. It would have to go back to the membership, itself, and they, too, would pay income tax on that.

Mr. SHIMKUS. He is going to have to throw me out of the chair. I am going to move on. Thank you very much.

I move to the gentlewoman from the State of Missouri, Ms. McCarthy, for 5 minutes.

Ms. MCCARTHY. I thank the chairman, and I would like to thank the witnesses for their presentation today.

I would like to explore a concept with you that is still troubling to me as we move forward, and that is how, as we move forward into this new era of competition, do we achieve the efficiencies and also the environmental goals that we have obligated ourselves to worldwide?

My worst fear is that, as we open up competition, industry will look more and more to the cheapest sources of fuels in order to compete, those perhaps being the more traditional uses of coal and others that we know make our cities hard to breathe in and cause the EPA great concern as far as air quality.

Is there enough in this measure on encouraging uses of indigenous energies, those that are renewable and clean? Do we need to add a renewable portfolio standard, as we have sometimes talked about? Is the incentive program, as currently proposed, enough? And what about a public benefits fund so that we are encouraging conservation and low-income assistance, as well?

How do we set a standard in the world where we move to efficiency to lower costs for consumers, but also to a better environment?

I know, Mr. Hawkins, you spoke to this briefly in your testimony. I would like to begin with you, but I would like to hear from any other member of the panel who is interested in sharing these thoughts with us so that we can come together and propose language that would make this work.

Mr. HAWKINS. Well, thank you, Congresswoman McCarthy.

Yes, our coalition of organizations supports three critical environmental measures: the public benefits trust that you mentioned, to support existing investments in efficiency, low-income services, and other public benefits; the renewable portfolio standard—both of those will be addressed in the second panel; and, finally, achieving an environmental performance cleanup.

On that last point, the way I would try to answer your question is the way that this industry will be incented to improve its performance is by making good performance valued in the marketplace.

In my testimony, I point out today's situation, which is problematic. An entrepreneur that wants to build a new high-efficient, clean power plant goes to investors, and that entrepreneur can point out that the power plant may emit very little sulfur dioxide, may emit very little or no mercury, may emit far below the required control levels for nitrogen oxides, and may emit much less CO_2 than other competitors.

But the investors are not interested in that. Investors are interested in what is your bottom line bus bar costs and how does it compare to your competition. And if your competition is an old grandfathered power plant that is able to continue to burn dirty fuel because of balkanized pollution control rules, the investor says, "Sorry. Great idea. Come back later." And the plant doesn't get built.

So the way to deal with this is to put a generation performance standard in the law which treats all generators equally, and says, "When you produce a megawatt hour of electricity, that is a useful social service and you are going to get a certain allocation of pollution allowances to meet those needs." Now the entrepreneur comes in, has this super-clean plant, and he or she can say to the investor, "When I generate a megawatt hour of electricity, I am generating an additional revenue stream because I am going to have credits that can be sold into the market, and that really makes my investment a more-attractive opportunity for you," and that will tend to make the answer be yes to build that plant.

Ms. MCCARTHY. Thank you.

Ms. Church?

Ms. CHURCH. I think, generally, that enactment of comprehensive wholesale legislation will benefit the environment. We would

certainly like to see, over time, comparability between the older and the newer plants, and we definitely believe that, where credits are being allocated, that newer entrants do need to have an opportunity to get those credits and they need to be reallocated periodically.

And on renewables, we do think that there are some amendments that could help strengthen the bill. The current bill tries to provide symmetry between the tax credits that are already in the law and benefits to public power.

There are still a number of renewable sources that fall through the cracks on that attempted symmetry, and we do think some refinements are needed there.

Ms. MCCARTHY. I thank you. And I see that I have run out of time. Thank you, Mr. Chairman.

Mr. SHIMKUS. Thank you. And I recognize the chairman of the subcommittee, Chairman Barton, for 5 minutes, or however long as he wants to take.

Mr. BARTON. No, no. Five minutes.

Just an observation before I start my questions. I used to sit out in the audience during the natural gas debate in the early 1980's about decontrolling natural gas, both in the House and in the Senate, and I felt I knew the answer and I was so smart, and if those ignorant Senators and Congressmen would just let me do it, we could solve that problem. And now I am over here and I wish I was over there, because I feel like, you know, what are we going to do, because everybody that has testified today has had some very good points.

So I used to be a lot smarter when I was sitting out there than I am when I am sitting up here.

Let me start off with an easy question. The current draft before us has a distributed generation size cap of 50 megawatts. We are told by a lot of people that is a little bit too large. Is there a better number, Mr. Owens, that you would like to see our third draft go to on distributed generation?

Mr. OWENS. Well, I certainly think 50 megawatts is just an extreme. I do not have a specific number, but I think if you we going to start, you certainly should start at something significantly scaled down. Let's say perhaps five megawatts could be an upper limit.

Mr. BARTON. Five to ten. Mr. Richardson, do you have a position, your group have a position on that?

Mr. RICHARDSON. Mr. Chairman, my group does not have a position. I was struck at the size of 50 megawatts when I first read through H.R. 2944. It seemed to me to be quite large.

Mr. BARTON. Okay. Let me ask you a question, Mr. Richardson, again on market power.

Mr. RICHARDSON. Yes, sir.

Mr. BARTON. Yesterday, the Clinton administration's witness, the deputy secretary of Energy, really enforced upon the subcommittee that we needed to take the Administration's provision on market power, which would allow the FERC to require forced divestiture.

I am not of that persuasion. I think you know that, having come to our working group. I am concerned about, if there truly is market power, we need to do something, but I do not see why the

States are not the solution. Didn't California have market power provisions in their State law?

Mr. RICHARDSON. They have divestiture requirements.

Mr. BARTON. But it was a State decision?

Mr. RICHARDSON. Yes, it was a State decision.

Mr. BARTON. Doesn't Texas have market power provisions in its law?

Mr. RICHARDSON. Yes.

Mr. BARTON. Okay. Doesn't Pennsylvania?

Mr. RICHARDSON. I am not that familiar with Pennsylvania's legislation, but I believe you are correct.

Mr. BARTON. Just for the subcommittee's edification, we are going to address market power. If we need to put a political fix in, so be it, but, before we decide on a political fix, we ought to really look at what is happening in the States, and every State that has acted in some fashion has addressed market power, and we really should think carefully, in my opinion, before we put a Federal fix on market power in if the States are taking—are already handling that.

Now, Mr. Richardson, you said something that really struck me. You did not give a specific example. You said you did not want to burden the subcommittee with more paper. Well, burden us. If you know of a specific example where a utility generator withheld generating capacity at a critical period simply to drive the price up and exercised market power, I would like to know that.

Mr. RICHARDSON. We will give you examples of the combination of the abuse of transmission and generation.

Mr. BARTON. Well, your specific example, though, was you talked about horizontal generation power, where a particular utility could withhold generation from the system to—I think you used the word "game" the system.

Now, I know we have had some transmission bottlenecks. I am familiar with most of those. I won't claim I am familiar with all of them. But I have not heard before somebody make the allegation that a generator withheld generating capacity during a peak period, and I would be interested in it, and I know former Chairman Dingell would be interested in it. That is one of his big concerns. So we would really like to have that.

Now, Mr. Hawkins, I want to ask you a question. You are the witness that says we ought to put in some Clean Air Act provisions for the grandfathered power plants. If we do not put those in, are you going to recommend a vote against any bill?

Mr. HAWKINS. We certainly will look at the entire bill, and if the bill does not contain provisions which provide assurances that this restructured industry will protect the environment, then yes, we would recommend the members to vote against the bill.

Mr. BARTON. My understanding is, under the current Clean Air Act, we have Federal standards. We do grandfather some of these older power plants that burn some of the coal.

Could a State put in a tighter standard on those grandfather plants, or does the Clean Air Act preempt that?

Mr. HAWKINS. A State could put in a standard as a matter of law. The problem is that the State could not protect its air quality just by regulating the sources within its State.

Mr. BARTON. My point is, under the current Clean Air Act, if that is a problem, the State of Ohio, to pick a name out of the air, or the State of Illinois, to pick another State out of the air, they could set tighter standards for those plants, could they not?

Mr. HAWKINS. They could, but they would be ineffective because——

Mr. BARTON. But they could do it? They could do it. The answer to that is yes.

My time has expired and I yield back to the gentleman from Illinois.

Mr. SHIMKUS. Thank you. And, for Mr. Richardson, if you would provide that information.

Mr. RICHARDSON. We will do that.

Mr. SHIMKUS. I just wanted to get the commitment on the record that you would provide that information to the chairman.

Mr. RICHARDSON. Yes.

Mr. SHIMKUS. Now I recognize the gentleman from Florida, Mr. Stearns, for 5 minutes.

Mr. STEARNS. Thank you, Mr. Chairman.

This is directed to Lynne Church. Just a clarification. I think earlier staff indicated that you made the assertion that, I think in the PURPA language that I have, it does not explicitly protect existing contracts; is that true?

Ms. CHURCH. I said that in my written testimony. Correct. Yes.

Mr. STEARNS. I just wanted to read from page 79 of the bill that I have that says, ''Existing rights and remedies not affected,'' page 79—''Nothing in this section affects the rights or remedies of any party with respect to the purchase or sale of electric energy or capacity from or to a facility determined to be a qualifying small power production facility,'' and so forth.

And it says, ''Pursuant to any contract or obligation to purchaser to sell electric energy or capacity in effect on the date of the enactment of this act.'' So——

Ms. CHURCH. Well, we would like to see some language that specifically provides symmetry between protection of the utilities for their recovery of stranded costs that are tied to above-market PURPA contracts with the obligation, therefore, to continue to supply to pay under the existing contract.

Mr. STEARNS. Well, from what I just read to you, it appears that they have these remedies in place in the bill that I have, so, I mean, I think your initial statement might not be correct. Do we agree on that?

Ms. CHURCH. We will certainly look at it again, sir.

Mr. STEARNS. Okay. You proposed granting FERC jurisdiction over transmission used to make bundled retail sales.

Ms. CHURCH. Correct.

Mr. STEARNS. What is the position of the States on this issue?

Ms. CHURCH. NARUC has filed comments that, as I understand it, disagree, and I think that the reason that we believe it is very, very important is that, while the States are very well-meaning—and I certainly do not attribute any malevolence to their view—they are taking—they tend and have the opportunity, under the way the law is being interpreted, to take very parochial views, which can have the impact of adversely impacting neighboring

States, and certainly preventing the market from operating the way it should.

The example I would use is the one that underlies the Northern States Power case, the 8th circuit case, which I think has brought this to the fore, where the Minnesota law required the utility to curtail a firm transportation contract on its transmission system in order to protect its "native load." Well, the contract that they curtailed was, in fact, power that was moving to the next State, Wisconsin, to serve their native load.

And so what we need to realize is that the system, even now, and even more so in the future, as States open up, is going to be relied upon to serve residential customers.

And I think the second view that there is general misunderstanding, both sometimes on the Commission's level and in the general public, that curtailment of transmission automatically is going to end up turning off the lights. That is not correct.

What it really means is that sometimes, where a contract is curtailed, the recipient of that contract is going to have to go into the hourly market for more expensive power, but most times it does not mean the lights actually go out.

Mr. STEARNS. Mr. Richardson, you say that H.R. 2944 eviscerates FERC's jurisdiction over the transmission system. Now, this is not what FERC told us yesterday. FERC told us that H.R. 2944 codifies Order 888. So let's be clear what you are asking here.

You want Congress to go beyond Order 888 and give FERC jurisdiction over a larger part of the transmission system than it is asserted in Order 888? Is that not correct?

Mr. RICHARDSON. I do not believe so, Mr. Chairman.

There are a couple of issues here. One, I, frankly, get rather confused when I look in that language in that section, bundled and unbundled services. There are a couple of problems that we have with——

Mr. STEARNS. Just let me interrupt you for a second.

Mr. RICHARDSON. Yes, sir.

Mr. STEARNS. Just the way I laid the question out, do you agree or not? Do you want me to read it again?

Mr. RICHARDSON. Well——

Mr. STEARNS. In other words, my question——

Mr. RICHARDSON. Yes. Please do.

Mr. STEARNS. Is that not correct? You are saying that——

Mr. RICHARDSON. Second part, Mr. Stearns, the refunctionalization issue that I mention in my testimony gives the utilities the opportunity—and I think it is pretty well documented in another item that I included with my testimony—to remove facilities that are currently FERC jurisdictional by refunctionalizing them from the function of transmission to the function of distribution.

Now, that certainly diminishes the authority of the Commission over facilities with respect to which they currently do have jurisdiction.

Mr. STEARNS. Okay. Has FERC been approving those classifications?

Mr. RICHARDSON. I am not sure of the status of those classifications. The language of the—I can give you instances, for example, in Wisconsin of a proposal to take nearly 80 percent of trans-

mission out of FERC's jurisdiction, converting it to State jurisdiction. There are other examples in the article that I presented.

Of particular concern to us is the requirement that FERC defer to those State commission decisions, and, as I believe Ms. Church said a moment ago, there are concerns about parochial treatment.

Mr. STEARNS. Okay. Mr. Chairman, my time has expired.

I thought I would bring to the attention of the committee a "USA Today" advertisement on Friday, September 17, in which there is probably no need for electric if this is true. It says, "Tired of high electric bills? How about no electric bills? This machine will give you free electricity for the rest of your life."

Mr. RICHARDSON. I will take two.

Mr. STEARNS. It says it capitalizes upon the fourth law of motion—now, to my knowledge there are only three—and it utilizes energy previously thrown away so that you will have free electricity for the rest of your life. So if anybody wants a copy of this ad, here is an opportunity for free electricity.

Mr. BARTON. TVA will be selling those in the lobby.

The gentleman from Mississippi, Mr. Pickering. Five minutes. Questions only.

Mr. PICKERING. Thank you, Mr. Chairman.

Let me just ask a number of the panelists the same question. Let me first start with Mr. English.

Upon reviewing the draft in its current form, could you support or would you oppose, and what are the three primary concerns that you have with the legislation in its current form that would need to be addressed to obtain your support if you do not support it at this current time?

Mr. ENGLISH. As I stated in my previous testimony, Mr. Pickering, the thing that we are most concerned with is unnecessary regulations with regard to achieving the goals pertaining to the question of the regulatory burden under FERC. We do have concerns. We do not really think it makes much sense as far as merger authority under FERC.

We are concerned that in a restructured environment that we have, in effect, electric cooperatives be able to provide all the services that any other electric utility can provide, and also we want to make sure electric cooperatives can work together to be able to provide and meet the same needs, particularly from a billing standpoint, that other electric utilities can.

Mr. PICKERING. Just a quick follow-up. How many of your States or how many of your co-ops operate in States where there is no State regulatory authority or jurisdiction at the present time?

Mr. ENGLISH. I would need to submit that for the record, but roughly—I had better submit it for the record. I think it is half to three-fourths, somewhere in that neighborhood.

Most States view electric cooperatives from the standpoint that, since they are consumer-owned, they elect their own board of directors from the consumers, they regulate themselves, unlike other utilities.

Mr. PICKERING. It has actually been a pretty good system, hasn't it?

Mr. ENGLISH. Worked extremely well. I am not aware of complaints from States that provide for this process.

Mr. PICKERING. I believe Mississippi is one of those.

Mr. ENGLISH. It is, indeed.

Mr. PICKERING. Let me ask Ms. Church the same question that I first asked Mr. English.

Would you support or oppose the current draft? And what are the three primary things that would need to be addressed if you do not currently support the legislation?

Ms. CHURCH. We believe, as I said before, there are a lot of things in the bill that we really like; however, the three provisions that we think give State commissions an undue opportunity to intrude onto the interstate grid may lead us to a position where we would not be able to support.

We do believe that those provisions, particularly the distinction between bundled and unbundled, is a critical flaw in the bill.

Mr. PICKERING. And would you currently support the legislation?

Ms. CHURCH. We certainly support the passage of legislation. We think it is needed. But we do think this bill does need some revisions.

Mr. PICKERING. Mr. Owens, would you support or oppose the current draft?

Mr. OWENS. I think the current draft needs some refinements, and I would put them in probably two large categories. One large category, I am certainly very troubled by the aspects that deal with public power, the TVA, the Bonneville, the co-op revisions, and the municipal provisions.

New generation and transmission should be subject to the same rules. Subsidies should not be used to distort the marketplace, so I would suggest a major improvement in that area.

The second area that I am troubled about is the expansion of FERC's authority, particularly with respect to the merger provisions. I particularly believe it is unnecessary to have FERC dabble in the area of retail competition issues. Similarly, I do support flexibility in regional transmission organizations.

And then, finally, I have some difficulty with the net metering requirements in the bill which could be fine-tuned, as well as the aggregation aspects, and then the inter-connection requirements, the 50 megawatt standard and the requirement that FERC can require that the distribution system be expanded.

Mr. PICKERING. Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Mr. Pickering.

Mr. Wynn has arrived, and so we will yield to Mr. Wynn 5 minutes for questions.

Mr. WYNN. Thank you, Mr. Chairman.

Unfortunately, I did not have the opportunity to hear the testimony, so it would probably be presumptuous to start asking questions. I will defer.

Mr. BARTON. It would be very Congressional for you just to pitch right in.

Mr. WYNN. I am going to try to start a new precedent.

Mr. BARTON. An informed questioner. How about that?

Is Mr. Ehrlich here?

Mr. SHIMKUS. He has left, Mr. Chairman.

Mr. BARTON. Okay.

Mr. SHIMKUS. Mr. Chairman, may I just ask that we can get some more questions submitted on the record——

Mr. BARTON. Yes.

Mr. SHIMKUS. [continuing] for written response from the panelists?

Mr. BARTON. Yes. We are not going to do a second round of questions.

Mr. SHIMKUS. Right. I understand.

Mr. BARTON. Okay.

Congressman Tauzin asks unanimous consent on his behalf to submit a statement for the record. Is there objection to all members of the full committee, not just the subcommittee, being given unanimous consent to put a statement in the record on this issue?

[No response.]

Mr. BARTON. Hearing none, so ordered.

Let me, before I release this panel, reiterate what I said at the beginning.

We are going to have one more panel today. We are not going to go to markup next week because of the pending markup of the Superfund bill at the full committee, but it is the Chair's intention, again, in consultation with Chairman Bliley and Mr. Hall and Mr. Dingell, to try to schedule a markup the week after that. So, all of these concerns that have been expressed by this particular panel, we encourage you to do two things: No. 1, put them in legislative language; No. 2, find a champion on the subcommittee, preferably two champions, one on the republican side and one on the democrat side, and submit them—get your champions working, and then submit the language to Congressman Hall and myself so we can review it, because I do intend to put together a subcommittee substitute that we will mark up the week after next.

So the time has come to stop being concerned and start being constructive in putting these issues into language that the subcommittee members on both sides of the aisle can take a look at.

Again, thank you for your testimony. You are excused.

As soon as they have vacated the premises, we want to hear from our second panel.

Lady and gentlemen, we welcome you to the subcommittee. We are going to start with Mr. Brice and work our way through to Mr. Segal. Each of your statements is in the record in its entirety. We are going to recognize you to summarize it in 6 minutes, and we are going to start with Mr. Jack Brice, who is a member of the board of directors of the American Association of Retired—is it People or Persons?

Mr. BRICE. We just say "AARP" now. We changed the name legally.

Mr. BARTON. So it is just——

Mr. BRICE. But prior to that it was "persons."

Mr. BARTON. Persons. Okay. AARP. We could say "real people." How about that? Anyway, we welcome you, sir, and you are recognized for 6 minutes.

STATEMENTS OF RUTHERFORD "JACK" BRICE, MEMBER, BOARD OF DIRECTORS, AARP; ELIZABETH ANNE MOLER, GENERAL COUNSEL, AMERICANS FOR AFFORDABLE ELECTRICITY; MARK N. COOPER, DIRECTOR OF RESEARCH, CONSUMER FEDERATION OF AMERICA; MARTY KANNER, COALITION COORDINATOR, CONSUMERS FOR FAIR COMPETITION; RICHARD H. COWART, DIRECTOR, REGULATORY ASSISTANCE PROJECT; TOM SMITH, DIRECTOR, TEXAS PUBLIC CITIZEN; THOMAS R. CASTEN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, TRIGEN ENERGY CORPORATION; AND SCOTT H. SEGAL, ON BEHALF OF THE NATIONAL ALLIANCE FOR FAIR COMPETITION

Mr. BRICE. Good morning. We thank Chairman Barton and the other members of the committee for inviting us to present our views on the consumer protection provisions within H.R. 2944, the Electricity Competition and Reliability Act.

We will confine our remarks to the provisions contained in title III of the bill, as well as to the sections in title V dealing with aggregation. However, as representatives of residential consumers, we also share some of the concerns surrounding the market power provisions voiced by other panelists over the past 2 days.

In short, AARP wants to ensure that residential customers benefit from competition, that strong consumer protection provisions are in place, and that electric utility service is available to all.

AARP believes that residential customers should benefit from restructuring; unfortunately, residential customers are simply not as attractive to utilities as industrial customers are.

Mr. Chairman, we feel one means to strengthen the position of residential consumers is through aggregation. Aggregation will allow residential consumers to pool their respective electricity needs, enabling them to negotiate lower rates from a power provider and benefit from the outset.

AARP also supports a Federal role in facilitating aggregation in States that have opened their markets to competition.

H.R. 2944 recognizes the importance of aggregation, as well.

The bill provides residential consumers with flexibility, allowing that any entity that aggregates consumers may acquire retail electric energy on an aggregate basis.

As we have suggested before, residential consumers would further benefit if aggregation was offered on an opt-out basis. The opt-out provision would ensure that a majority of under-served consumers could reap the benefits of lower rates.

For competition in the electric industry to work, strong consumer protection laws must be applied to the sale of electricity in restructured industry. We are pleased that title III of H.R. 2944 is devoted to addressing consumer protection concerns.

Mr. Chairman, the anti-slamming and anti-cramming provisions will go a long way toward addressing these abuses.

AARP is also pleased that the need for information disclosure is increasingly understood by policymakers and reflected in H.R. 2944. The bill includes provisions outlining the kind of information that supplies must present to consumers when offering services. Many of the details that we have urged to be included in billing statements are included in this section.

Further, the legislation clarifies that States may impose additional requirements. This kind of consumer information floor is what we have been seeking.

Further, we applaud Chairman Barton for striking a delicate balance between the protection of individual privacy and the need to make aggregate consumer information available to promote competition.

AARP values the individual's right and ability to control the movement of personal information. We are pleased that provisions in H.R. 2944 recognize that right by requiring prior written approval before personal information can be disclosed.

We also support the provision in H.R. 2944 that requires local distribution companies to make aggregate consumer information available to retail electric suppliers upon request.

By facilitating the transfer of this type of information, residential consumers are more likely to be offered choice.

While we are pleased overall with the consumer protection provisions included in H.R. 2944, AARP would still like to see a truth in billing requirement adopted to supplement the information disclosure provision. AARP is concerned that, in a competition environment, less-attractive customers will be adversely affected.

H.R. 2944 recognizes universal service through a sense of Congress, but places the full burden on a State to collect fees and implement the program.

AARP believes that there is still a role for the Federal Government in ensuring that electric service is provided to all consumers.

AARP is pleased with the attention Chairman Barton has devoted to residential consumers in H.R. 2944. The consumer protection and aggregation provisions should benefit consumers, but only if adequate market power provisions are put into place to ensure that competition becomes a reality.

And, finally, AARP hopes that, as legislation moves toward passage in the House, the provisions we have discussed today remain intact or are improved. We urge this committee to remember that residential consumers will benefit from restructuring only if aggregation is facilitated, strong consumer protection provisions are enacted, and electric service is ensured for all.

Again, Mr. Chairman, we thank you for inviting us to testify.

[The prepared statement of Rutherford "Jack" Brice follows:]

PREPARED STATEMENT OF RUTHERFORD "JACK" BRICE, MEMBER, BOARD OF DIRECTORS, AARP

Mr. Chairman and Members of the Committee: My name is Jack Brice and I am a member of AARP's Board of Directors. We thank Chairman Barton and the other members of the Committee for inviting us to present our views on the consumer protection provisions within H.R. 2944, the "Electricity Competition and Reliability Act." We will confine our remarks to the provisions contained in Title III of the bill as well as to the section in Title V dealing with aggregation. However, as representatives of residential consumers we also share some of the concerns surrounding the market power provisions voiced by other panelists today.

AARP's membership has a vested interest in the move towards competition now underway in the electric utility industry. For everyone, electricity is a basic necessity of modern life. The cost of this necessity, however, can comprise a significant portion of an average consumer's personal expenditures. In fact, energy costs can take up to as much as 5 percent of the median-income household's monthly budget. Older Americans are particularly vulnerable to rapid increases in energy prices. Although older persons consume approximately the same amount of residential energy

as non-elderly Americans do, they devote a higher *percentage* of total spending to residential energy. Among low-income older families, an average of 17.5 percent of their income is spent on residential energy. Too often, low-income older persons are faced with the choice of risking their health and comfort by cutting back on energy expenditures or reducing spending for other basic necessities.

In testimony AARP presented to this Committee earlier this year we discussed generally our concerns surrounding the move to retail competition. We questioned the claims that retail competition would bring about substantial rate reductions for all ratepayers, including the elderly. We also expressed hope that consumers would receive the corollary benefits of the ability to shop among competitive providers, and to take advantage of a new array of products and pricing options. We concluded that the fate of residential consumers in a restructured electric industry will depend on whether the new market structure gives them a fair chance to receive the benefits of competition, ensures that their interests are represented in the market, and provides fundamental protections against abuse.

Residential ratepayers, and particularly older Americans, face very significant risks—and few, if any, assured benefits—in the move to retail competition in the electric power industry. These risks go beyond the ability to benefit from choice. They also include risks associated with confusion, deception and fraud.

AARP is pleased that H.R. 2944 addresses these risks. Our testimony today will focus on how elements of Chairman Barton's bill support AARP's goals to:

- Ensure that residential customers are among the first to benefit from competition;
- Provide strong consumer protection provisions; and
- Establish a comprehensive universal service policy, including a guarantee of affordability.

Residential Customers First

AARP believes that residential customers should benefit from restructuring. Unfortunately, residential consumers are simply not as attractive to utilities as industrial customers are. Discussions between AARP staff and representatives of electric utilities, industrial consumers and regulators have highlighted the fact that residential consumers are not likely to reap the full benefits of restructuring during the initial years of competition. The ability to aggregate, however, will help to bring some benefit in the short-term.

Aggregation will allow residential consumers from like communities or associations to pool their respective electricity needs, enabling them to negotiate lower rates from a power provider and benefit from the outset.

AARP supports a federal role in facilitating aggregation in states that have opened their markets to competition. H.R. 2944 recognizes the importance of aggregation as well. The bill provides residential consumers with flexibility, allowing that any entity that aggregates consumers may acquire retail electric energy on an aggregate basis. As we have suggested before, residential consumers would further benefit if aggregation were offered on an opt-out basis. The opt-out provisions would ensure that a majority of underserved consumers could reap the benefits of lower rates. Rep. Brown has introduced the concept of a residential opt-out aggregation system in his "Community Choice for Electricity Act of 1999."

Consumer Protection Laws

For competition in the electricity industry to work, strong consumer protection laws must be applied to the sale of electricity in a restructured industry. Low-income, non-English speaking and elderly consumers, in particular, will need very strong consumer protections to prevent abuse in the competitive market.

We are pleased that Title III of H.R. 2944 is devoted to addressing consumer protection concerns. Attacking the problems of slamming and cramming, while providing for information disclosure and privacy restrictions is to be commended.

If enacted, the anti-slamming and anti-cramming provisions of the Chairman's legislation will go a long way towards addressing these abuses.

AARP is pleased that the need for information disclosure is increasingly understood by policymakers and is reflected in H.R. 2944. The bill includes provisions outlining the kind of information that suppliers must present to consumers when offering services. Many of the elements that we have urged be included in billing statements, such as price information, description of charges, and information regarding interruptibility of service are included in this section. Further, the legislation clarifies that states may impose additional requirements. This kind of "consumer information floor" is what we have been seeking.

Further, we applaud Chairman Barton for striking a delicate balance between the protection of individual privacy regarding information exchange and the need to make aggregate consumer information available to promote competition. AARP val-

ues the individual's right and ability to control the movement of personal information. We are pleased that the provisions in H.R. 2944 recognize that right by requiring prior written approval before personal information can be disclosed.

We also support the provision in H.R. 2994 that requires local distribution companies to make aggregate consumer information available to retail electric suppliers upon request. By facilitating the transfer of this type of information, residential consumers are more likely to be offered choice.

While we are pleased overall with the consumer protection provisions included in H.R. 2944, there are certain areas that need further attention. In earlier testimony we detailed the importance of adopting a "Truth-in-Billing" requirement to supplement the information disclosure provision. AARP suggested that a comprehensive, easy-to-read billing statement each month would help alleviate consumer confusion, making consumers more likely to become participants in the competitive marketplace. This provision is missing from H.R. 2944.

AARP also supports the creation of a consumer database housed at the FTC to assist residential customers in obtaining information about retail electric utility providers, including aggregators. Additionally, the creation of an Office of Consumer Counsel within the FERC, as outlined in an earlier draft, would assist consumers.

Finally, as large aggregators, utility companies and power marketers are likely to operate on an interstate basis, it is incumbent upon the Congress to ensure that they meet certain threshold operational requirements and that deceptive, fraudulent or other illegal behavior not be not tolerated.

Universal Service

As we have said previously, electric utility service is essential. Therefore, one of the cornerstones in any restructuring effort is the requirement that electric utility service be universal and affordable. A universal service policy must ensure basic electric service at a level of consumption that would meet the needs of residential ratepayers for lighting, heating, cooling, cooking, and recreation. In our view, affordability means that electricity rates do not strain the household budget.

AARP is concerned that in a competitive environment, less attractive customers may be adversely affected. H.R. 2944's only recognition of universal service is through a "Sense of the Congress" provision. Unfortunately, such a declaration places the full burden on the states to collect fees and implement the program. AARP believes that there is still a role for the federal government in ensuring that electric service is provided to all consumers. At a minimum, federal involvement should include participation on a Federal-State Joint Board that would oversee a program funded by a fee placed on all generators of electricity.

Conclusion

AARP is pleased with the attention Chairman Barton has devoted to residential consumers in H.R. 2944. The consumer protection and aggregation provisions should benefit consumers, but only if adequate market power provisions are put in place to ensure that competition becomes a reality.

AARP hopes that as legislation moves toward passage in the House, the provisions we have discussed today remain intact or are improved. We urge this Committee to remember that residential consumers will benefit from restructuring only if aggregation is facilitated, strong consumer protection provisions are enacted and electric service is ensured for all.

Mr. Chairman, the work that you have done to highlight many of the inherent problems in the move to a deregulated environment is to be commended. H.R. 2944 is a big step in the right direction. AARP looks forward to continuing our active participation in this debate on both the federal and state level and to working with you in crafting solutions that will ultimately benefit not only our members, but the nation as a whole.

Mr. BARTON. Thank you, Mr. Brice.

We would now like to hear from The Honorable Betsy Moler, the general counsel for Americans for Affordable Electricity and a former deputy secretary of Energy and commissioner at the FERC.

Ms. Moler?

STATEMENT OF ELIZABETH ANNE MOLER

Ms. MOLER. Thank you, Mr. Chairman and members of the subcommittee. It is a pleasure to be before the subcommittee again today.

I am testifying on behalf of Americans for Affordable Electricity, or AAE. AAE is a diverse coalition of over 200 member organizations. Their common bond is support of a more competitive electric marketplace. We appreciate the opportunity to testify.

AAE believes there is an urgent need for Congress to enact legislation to modernize the laws governing this Nation's electricity business. Many of the laws currently on the books, as you have recognized, Mr. Chairman, are impeding progress toward a more-competitive electric marketplace.

AAE supports customer choice. Since Chairman Bliley took customer choice off the table, as he said, as a legislative priority in this Congress, we have turned our focus to improvements in the wholesale electricity marketplace that will further competition.

My testimony today focuses on wholesale issues; however, I do want to reiterate our support for customer choice, as well as legislation that would give all customers the right to aggregate their electricity purchases, whether or not they are located in States that provide customer choice.

We believe that H.R. 2944 is a well-intentioned piece of legislation; however, we do not support enacting it in its current form because we believe it will serve to inhibit competition, rather than to promote it.

In the brief time I have today, I want to focus on one aspect of H.R. 2944 that is particularly troublesome, the transmission jurisdiction provisions.

Section 101 purports to clarify the respective role of Federal and State jurisdiction, but in doing so it creates new barriers to competition. We need to have all transmission under one set of rules, and we need to separate the transmission function from the sales function in order to make electricity markets more open and competitive.

Let me explain.

Section 101 clarifies that FERC has authority over unbundled transmission of electric energy sold at retail, while State regulatory authorities have authority over any bundled sale of electric energy. This same standard is being applied today, although it is being challenged in the DC circuit litigation over Order 888.

In Order 888, FERC determined it had jurisdiction over so-called "unbundled transmission" in interstate commerce by public utilities. Thus, in States that have adopted customer choice, the use of the transmission facilities is under FERC's jurisdiction. However, the same type of facility is not under FERC's jurisdiction in States that have not adopted customer choice.

What does this mean in the real world? You have a crazy quilt of jurisdictional lines. FERC has authority over transmission lines in States that have adopted customer choice, while State regulators have authority over exactly the same type of facilities in States that have not adopted customer choice.

Virginia, for example, has adopted customer choice legislation, while West Virginia has not. The Virginia transmission lines are subject to Federal regulation, while the West Virginia lines are not.

This simply does not make sense any more. All transmission lines that are part of the interstate network must be under FERC's jurisdiction and subject to the same type of open access require-

ments. Split jurisdiction over the interstate grid simply does not make sense.

Based upon experience since Order 888 was issued, AAE firmly believes that we need to put all uses of the interstate transmission grid under the same rules. The same open access tariff should apply to wholesale transmission transactions and to both bundled and unbundled retail transmission.

We have submitted legislative language with my testimony today to treat all transmission lines the same, whether they are used for bundled or unbundled retail sales.

Let me explain and emphasize this is not back-door customer choice. The text of the amendment makes it very clear FERC does not have any authority to require customer choice. That choice would remain with the States.

The amendment addresses two other issues we believe are also critical. First, it would require all uses of the transmission system to be under the same open access tariff. Utilities would be required to take service under an Order 888 type tariff just like everyone else. That is not the case today.

Second, it would require utilities to separate their transmission and electric sales functions.

This approach is not some wild idea that we dreamed up overnight. It is the same approach that FERC applies now for natural gas pipelines.

Order 636 put all shippers under the same tariff and required pipelines to separate their transmission and sales functions. It works.

The proposal dovetails with the reliability section of the bill. Frankly, I cannot reconcile the reliability section with the provisions in section 101 that limit FERC's authority over transmission lines.

Nothing is more critical to the Nation's economic well-being than a reliable power supply. This is a classic interstate commerce issue.

Individual States cannot guarantee reliability of the interstate grid. FERC must have the authority to do so.

We urge the subcommittee members to take an evenhanded approach to writing this vitally important piece of legislation. We support restructuring legislation that will address these anachronistic laws such as PUHCA and PURPA, provided that new mechanisms are put in place to encourage open competitive markets.

Thank you for allowing AAE to testify.

[The prepared statement of Elizabeth Anne Moler follows:]

PREPARED STATEMENT OF ELIZABETH ANNE MOLER ON BEHALF OF THE AMERICANS FOR AFFORDABLE ELECTRICITY

Mr. Chairman and Members of the Subcommittee: It is an honor to appear before you today. My name is Elizabeth Anne Moler. I am a partner in the law firm of Vinson & Elkins, L.L.P. I am testifying today on behalf of Americans for Affordable Electricity, or AAE. AAE represents over 260 member organizations; their common bond is support of more competitive electricity markets. The diverse coalition includes commercial, residential and industrial energy consumers, utility and non-utility generators, power marketers, other energy providers, citizens groups, school administrators, and others.

We appreciate the opportunity to testify on H.R. 2944, Chairman Barton's recently introduced Electricity Competition and Reliability Act.

AAE believes there is an urgent need for Congress to enact legislation to modernize the laws governing this Nation's electricity business. Much has changed since

1992 when Congress passd the Energy Policy Act. Since then, events in the marketplace, and actions undertaken by both Federal and State regulators have partially reshaped this vital industry. Now inaction by the Congress is frustrating further progress toward an even more reliable, efficient, competitve industry for our Nation. Many of the laws currently on the books are impeding progress toward a more competitive electricity marketplace.

AAE supports customer choice. We favor legislation that would give all customers the right to choose their electricity supplier by a date certain. Since Chairman Bliley took customer choice "off the table" as a legislative priority for this Congress, we have turned our focus to improvements in the wholesale electricity marketplace that will further competition. Most of my testimony today focuses on wholesale issues. However, I want to reiterate our support for customer choice as well as legislation that would give all customers the right to aggregate their electricity purchases whether or not they are located in states that provide customer choice.

We believe that H.R. 2944 is a well intentioned piece of legislation. However, we do not support enacting it in its current form because we believe it will serve to inhibit competition rather than promote it. In the brief time I have today, I want to focus on one aspect of H.R. 2944 that is particularly troublesome. Section 101 purports to "clarify" the respective role of federal and state jurisdiction. But in doing so it erects new barriers to competition. We need to have all transmission under one set of rules. And we need to separate the transmission function from the sales function in order to make electricity markets more open and competitive. Let me explain.

Section 101 would clarify that the Federal Energy Regulatory Commission (FERC) has authority over "unbundled transmission of electric energy sold at retail" while state regulatory authorities have authority over "any bundled retail sale of eletric energy, to any local distribution service component of any unbundled retail sale of electric energy, or to any retail sale component of any unbundled retail sale of electric energy".

What would this mean in the real world? You would have a crazyquilt of jurisdictional lines where FERC would have authority over transmission lines in states that have adopted customer choice, while the state regulators would have authority over exactly the same type of facilities in states that have not adopted customer choice. Virginia, for example, has adopted customer choice legislation while West Virginia has not. The Virginia transmission lines would be subject to Federal regulation while the West Virginia lines would not. It would make more sense to have all transmission lines that are part of the interstate network be under FERC's jurisdiction and subject to the same type of open access requirements. Split jurisdiction over the interstate grid just doesn't make sense.

Frankly this crazyquilt exists today and is causing significant problems in wholesale markets. FERC Order No. 888, issued in April, 1996, required utilities to "open up" their transmission lines. They were required to file open access transmission tariffs and to take transmission service for their own new wholesale sales under the tariff. The Commission determined that it had jurisdiction over so-called "unbundled" transmission in interstate commerce by public utilities. Thus, in states that have adopted customer choice, the use of transmission facilities to serve retail customers is under FERC's jurisdiction. However, the same type of facility use is not under FERC's jurisdiction in states that have not adopted customer choice. (The Commission's determination that it lacked jurisdiction over the transmission aspects of bundled retail sales is being challenged today—3½ years later—in the Order No. 888 litigation that is before the D.C. Circuit.) Based upon our experience since Order No. 888 went into effect, AAE firmly believes that we need to put all uses of the interstate transmission grid under the same rules. The same open access transmission tariff should apply to wholesale transmission transactions, and to both bundled and unbundled retail transmission.

We are submitting an amendment as an attachment to my testimony that would treat all transmission lines the same, whether they are used for bundled or unbundled sales. Let me emphasize that this is not "back door" customer choice. The text of the amendment makes it very clear that FERC does not have any authority to require customer choice; that choice would remain with the states.

The amendment addresses two other issues that we also believe are critical. First, it would require all users of the transmission system to be under the same open access transmission tariff. Utilities would be required to take service under an Order No. 888-type tariff, just like everyone else. Second, it would require utilities to separate their transmission and sales functions.

This approach is not some wild idea that we thought up overnight. It is the same approach that FERC uses for natural gas pipelines. Order No. 636 put all shippers under the same tariff, and required the pipelines to separate their transmission and

sales functions. It works. States still have the authority to determine whether to adopt customer choice; some have while others have not. The natural gas marketplace is truly open and competitive. Congress should ensure that electricity markets are equally efficient and competitive.

This proposal will also enhance the usefulness and effectiveness of other provisions in H.R. 2944. This is particularly true for the reliability section. Title II gives FERC jurisdiction over a new electric reliability organization. The reliability organization is charged with the responsibility of developing binding reliability "organization standards" for the "bulk-power system".

Frankly, I cannot reconcile the reliability section with the provisions in Section 101 that limit FERC's authority over transmission lines. Nothing is more critical to the Nation's economic well being than a reliable power supply. This is a classic "interstate commerce" issue. Individual states cannot guarantee reliability of the interstate grid; FERC must have the authority to do so.

Section 103 requires all transmitting utilities to join a Regional Transmission Organization (RTO). AAE has not taken a position on this particular proposal. However, RTOs will be much more effective if FERC has authority over all transmission lines, not just those used for wholesale transactions and unbundled retail transactions.

The aggregation issue is also important. In the absence of a date certain for customer choice, AAE advocates allowing customers in both "open" and "closed" states to aggregate their purchases. The ABC grocery store chain, or the RAH RAH university alliance, should be able to aggregate their purchasing power to purchase electricity for multiple locations in multiple states. Without such a provision millons of residential and commercial customers will be unable to enjoy the benefits that competition will bring and H.R. 2944 should provide.

AAE supports legislation that will address these vitally important transmission market power issues. Our July 22 testimony addressed PUHCA, PURPA, grid management and reliability. Our position on those issues remains the same.

We urge the Subcommittee Members to take an even-handed approach to writing this vitally important piece of legislation. We support restructuring legislation that will address anachronistic laws, such as PUHCA and PURPA, provided that new mechanisms are put in place that encourage open, competitive markets.

Thank you for allowing AAE to testify.

Mr. BARTON. You are very welcome. We are just delighted that you testified, and we liked your testimony, actually. Do not agree with it all, but we liked the way you gave it.

We are going to hear from Mr. Mark Cooper, who is director of research with the Consumer Federation of America.

STATEMENT OF MARK N. COOPER

Mr. COOPER. Thank you, Mr. Chairman. And I also speak today on behalf of Consumers Union, who has signed onto our testimony.

With well over half the electricity in this Nation sold in States that have restructured their industry, consumers' electricity bills will be increasingly determined by the actual performance of markets. Unfortunately, the promise of lower prices and more choices at the State level is being undermined by the failure of the interstate market to support effective competition.

Only Federal authorities can order and oversee the interstate market, we believe, according to seven principles. We fear that the legislation before the committee will deregulate the industry without de-monopolizing it. Unless amendments are made, it will make matters worse, not better, because consumers will be denied the benefits of competition while they are subject to abuse of market power by incumbent utilities who are no longer restrained by regulation.

The seven principles are straightforward, and I will deliver these in seven sentences, because they are simple amendments.

Federal legislation should make a clear commitment to universal service, defined as the availability to all Americans of electricity services at rates that are just, reasonable and affordable.

Market power and generation must be eliminated. Federal authorities must ensure that generation markets are free of the exercise of market power. Simply put, antitrust authorities, who already have broad powers to oversee these markets, should make an affirmative finding that the market is competitive, workably competitive, before they are deregulated. Simple finding.

Third, open highways of commerce are necessary. The authority of the Federal Energy Regulatory Commission to require the national grid be operated in a reliable and open manner must be clarified and sharpened. All utilities should be required to participate in transmission organizations that have no interest in generation or energy service markets and include representatives of all customer classes.

Fourth, residential consumer sovereignty must be promoted. Federal legislation should require States to facilitate aggregation. At the very least, it should require that no State or local statute prohibit or hinder consumers from aggregating their purchase of electricity to all types of organizations, including cooperatives and units of local government.

Fifth, all consumers should benefit from competition. No utility should have the opportunity to enjoy the benefits of competition outside of its service territory until consumers within its service territory also have the benefits of competition. Before a company enjoys the benefits of being provided relief from Federal regulations, at home it should ensure that its own markets are open to competition. Competition is the replacement for regulation.

Sixth, financial transactions must be sound. Basic oversight has to be applied to financial transactions and commodity markets on a national basis, such as certification and licensing of brokers, and establishment of margin requirements, which should be imposed on electricity as a commodity, which is, in fact, a very, very special and precious commodity.

Seven, electricity restructuring should not result in any degradation in environmental quality. Congress should ensure that performance standards, portfolio requirements, whatever instruments you prefer should be available to ensure that, as a result of the increase in production from certain facilities, there is no resulting degradation in the environment.

Those are seven principles. I believe we can state those very, very clearly and specifically, and that is the way we think the interstate market should be——

Mr. BARTON. It was more than seven sentences though. I lost count at about 20. But they were seven principles.

Continue with your statement.

Is it concluded?

Mr. COOPER. Thank you, Mr. Chairman.

[The prepared statement of Mark N. Cooper follows:]

PREPARED STATEMENT OF MARK N. COOPER ON BEHALF OF CONSUMER FEDERATION OF AMERICA AND CONSUMERS UNION

Mr. Chairman and Members of the Committee, my name is Dr. Mark N. Cooper. I am Director of Research at the Consumer Federation of America. I appreciate the

opportunity to appear before you today to offer our views on federal legislation to restructure interstate electricity markets. Consumers Union joins in these views.[1]

LEGISLATION IS NECESSARY TO ENSURE EFFECTIVELY COMPETITIVE INTERSTATE MARKETS

With well over half the electricity in the nation sold in states that have restructured their industries, consumers' electricity bills will be increasingly determined by the actual performance of electricity markets. This unparalleled transition for an industry that is so vital to the national economy and has such a large impact on consumer pocketbooks must be made to result in a market that will truly benefit American consumers. Unfortunately, the promise of lower prices and more choices at the state level is being undermined by the failure of the interstate market to support effective competition.

In order for any market to function properly there must be an effective supply-side, an effective demand side, and open highways of commerce in between so that transactions can take place. The interstate market is failing consumers and competitors in all three areas. These market failures allow incumbent utilities to preserve their monopoly and frustrate the flow of competitive electricity.

The objective of restructuring is to replace traditional regulation with market forces. In many instances, however, consumers have been hurt because regulation has been removed before market competition exists. The result has been the unfettered exercise of market power. Evidence of the abuse of market power in interstate markets is abundant. Electricity has been withheld from markets to inflate prices. Electricity has been hampered from flowing across state borders by self-interested foreclosure of transmission facilities. Manipulation of financial transactions and speculative deals have driven prices far above reasonable levels at critical moments. Barriers have been erected by some states that prevent consumers from effectively expressing their demands in the marketplace.

Federal legislation is critically necessary to correct this series of dramatic failures. Only federal authorities can order and oversee the interstate market. The market must be restructured according to seven principles.

- A commitment to universal service
- Elimination of market power in generation
- A reliable national grid operated on principles of non-discrimination
- Meaningful choice for residential consumers
- Equal opportunity all consumers to benefit from competition
- Sound financial transactions
- Environmental preservation

UNIVERSAL SERVICE MUST BE ENSURED AND ENHANCED

The ultimate goal of restructuring in the electric utility industry should be to ensure and promote universal service in a more efficient manner than at present. Affordable and reliable service to the public is the ultimate goal; competition is the means to that end. Federal legislation should make a clear commitment to universal service defined as the availability to all Americans of a reasonable level of electricity service at rates that are just, reasonable and affordable.

MARKET POWER IN GENERATION MUST BE ELIMINATED

As the transition to competitive markets begins, incumbent utilities still dominate the generation market in many areas and at critical peak periods when supplies can become extremely tight. Federal authorities must ensure that the generation market is competitive and free from the exercise of market power. Antitrust authorities have broad powers to prevent the abuse of market power. The Federal Trade Commission should be required to make an affirmative finding that markets are workably competitive before federal regulatory authority is relaxed.

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[1] **Consumer Federation of America** is the nation's largest consumer advocacy group, founded in 1968. Composed of over 250 state and local affiliates representing consumer, senior citizen, low-income, labor, farm, public power, and cooperative organizations, CFA's purpose is to represent consumer interests before the congress and the federal agencies and to assist its state and local members in their activities in their local jurisdictions.

Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide consumers with information, education and counsel about goods, services, health, and personal finance; and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumer's Union's income is solely derived from Sale of Consumer Reports, its other publications and from noncommercial contributions, grants and fees.

OPEN HIGHWAYS OF COMMERCE ARE NECESSARY

At this point in time, many incumbent utilities still own generation and the transmission system, which provides opportunities for vertically integrated monopolies to use their market power in transmission to foreclose others from competing in the generation market. Separating ownership of generation from transmission and distribution is the best method of preventing abuses. Independent operation and control over the transmission network is necessary to ensure reliability and open, nondiscriminatory access to the transmission system for all parties.

The authority of the Federal Energy Regulatory Commission to require the national electricity gird to operate in a reliable and open manner needs to be clarified and sharpened. All utilities should be required to participate in transmission organizations that have no interest in generation or energy service markets and include representatives of all customer classes on the governing board. The infrastructure for the market must be competitively neutral and operated as a common carrier. The boundaries for these transmission organizations should be dictated by the scope of regional markets of sufficient scale to promote competition.

RESIDENTIAL CONSUMER SOVEREIGNTY MUST BE CREATED

In order for consumers to have the opportunity to benefit from the competitive marketplace for electricity they must have the ability to make informed choices. Aggregation is crucial to creating an alternative for residential consumers; education is crucial to effective choice.

Federal legislation should require states to facilitate aggregation; at the very least, it should require that no state or local statute should prohibit or hinder consumers from aggregating their purchases of electricity. Therefore, federal legislation should require that no state or local statute or regulation or other state or local legal requirement prohibit or have the effect of prohibiting the ability of consumers to aggregate their demand through all types of organizations including cooperatives and units of local government.

Instrumental in the ability of consumers to benefit from a competitive market is the ability to make informed choices. Information must be provided in a readily understandable manner that allows consumers to make comparisons between sellers in terms of price, terms and conditions (such as fees, contract terms and minimum payments), the services that are being provided and the type of electricity that is being used. Post-purchase remedies must be facilitated by clear identification of the seller, provision of a toll-free telephone number and policies to prevent abusive marketing practices, such as slamming, cramming and the bundling of regulated and unregulated services.

EQUAL OPPORTUNITY FOR ALL CONSUMERS TO BENEFIT FROM COMPETITION MUST BE PROVIDED

No utility should have the opportunity to enjoy the benefits of competing outside of its service territory until the consumers within its service territory have the opportunity to benefit from competition.

Before a company may enjoy the benefits of being provided relief from regulations intended to promote the public interest, such as PURPA and PUHCA, there should be a showing that the generation market in which they are based is competitive. If they are not subject to competition at home, the potential abuses that these statutes were intended to prevent remain a threat to consumers.

FINANCIAL TRANSACTIONS MUST BE SOUND

Markets must have confidence in the financial transactions that trigger the exchange of goods and services. The electricity market has been plagued by defaults, questionable deals (daisy chains) and misleading transactions. Prices have not been transparent. Terms and conditions have been unclear. Electricity is unlike most other commodities in that it cannot be stored and moves according to unique physical laws. When financial transactions break down, the electricity market can be severely disrupted.

The basic oversight that is applied to financial and commodity markets—such as certification, licensing and bonding of sellers, establishment of margin requirements, regulation of financial instruments and disclosure of transactions, publication of prices, etc.—should be applied to the electricity commodity market by an existing federal financial agency. A study of additional steps necessary to ensure the smooth functioning of the electricity market should be conducted.

ENVIRONMENTAL PRESERVATION

Electricity restructuring should not result in any degradation in environmental quality. Reliance on market forces may increase the use of generation resources that do not directly bear the full cost of the environmental burden they place on society (i.e. they impose negative external environmental costs). Congress should ensure, through performance standards, portfolio requirements, credit trading, or direct funding that environmental quality is preserved and improved.

Mr. BARTON. Okay. Thank you.

We want to now hear from Mr. Marty Kanner, who is the coalition coordinator for the CS for Fair Competition, which is different than the Americans for Affordable Electricity. See, we have all these good groups here before us today.

So we will put your statement in the record and encourage you to summarize it in 6 minutes, please, sir.

STATEMENT OF MARTY KANNER

Mr. KANNER. Certainly, Mr. Chairman. And, if nothing else, your efforts have fostered a plethora of organizations, coalitions, and initials.

I would like to start my testimony, Mr. Chairman, with the concluding statement from the executive summary of EEI's testimony. "As long as consumers have a choice of suppliers and no company can manipulate prices or shut out other competitors, consumers will find the best combination of prices and services to meet their needs." Mr. Chairman, I could not agree more strongly that that is exactly the end state that we seek to achieve. The difference, however, is quite sharp.

Edison Electric Institute and their members and many of their members and allies would argue that we simply step away and let the markets take care of themselves. I think we would all agree that the financial markets—the New York Stock Exchange is one of the best examples of free markets anywhere in the world, but I do not think we would say that Morgan Stanley, Michael Milken, and the Bass brothers should be able to regulate the system on their own; that we need the SEC as an oversight agency to ensure there is not market manipulation, consumer and investor abuse, or other things antithetical to that competitive end state that we seek to achieve.

A number of you have asked important questions that I would like to answer.

Mr. Shimkus asked whether RTOs can mitigate horizontal market power, and the answer, Mr. Chairman, is absolutely yes, but we need to make sure that those RTOs, in fact, are independent, have clear and robust authorities, and are of geographic scope that achieves the desired aim.

Mr. Chairman, the provisions in your bill I believe do not achieve that objective, because they allow the transmission owners to continue to set the rules of the market and do not have that independent authority to look at it and say, "No, not good enough." And then, second, as a number of witnesses have suggested, even if we create the perfect RTO, if we remove from the jurisdiction of those facilities a vast share of the transmission lines in the country, then we do not have that open highway of commerce that most of us believe is necessary.

Another question was whether there are examples of generation market power. The answers are clearly yes. In California, where they have opened retail markets, after doing so and where, Mr. Chairman, as you noted, generation assets were divested, you had substantial price increases, you had the State-created ISO and State-created power exchange, as well as the investor-owned utilities that used to own the generation go to the Federal Energy Regulatory Commission and say, "There is an exercise of generation market power." The State, itself, had no authority to control and regulate those price spikes, and, had there not been price caps in place, consumers would have seen a doubling of their monthly electric bills.

Those are the sorts of examples we want to avoid, not institutionalize.

You asked, Mr. Chairman, if States can do it alone, and you noted that a number of States have required asset divestiture. While that is true, I note that in the main the objective in those divestiture examples was to create evaluation for stranded cost recovery, not to address market power.

The effect was that assets were bundled and you just changed the name of the owner. You still had the same concentration levels in those relevant power markets. We did not divvy up the pie, if you will.

One important exception, however, is your State of Texas, where they expressly said, "We want to make sure that we have competitive generation markets," and created some mechanisms that I believe form a very workable model at the national level, that we say we want to make sure the generation markets are competitive.

Have the utilities file their own mitigation plans, and then have an impartial third party look over those and determine whether they are acceptable or not.

Mr. Chairman, I would encourage you to provide for all consumers the competitive benefits and choices that it looks like consumers in Texas will be able to have.

Mr. Chairman, as it has been noted by several witnesses, we need legislation. The current market is not properly functioning, and those retail markets that have opened up won't realize the benefits that those States tried to create if we do not, in fact, have a competitive market structure.

Consumers for Fair Competition has put together model legislation to address these issues. We would encourage you and your staff to review those and work cooperatively with us and the members of the committee to make sure that the intended benefits of a competitive market are, in fact, realized.

[The prepared statement of Marty Kanner follows:]

PREPARED STATEMENT OF MARTY KANNER ON BEHALF OF CONSUMERS FOR FAIR COMPETITION

Mr. Chairman, Members of the Subcommittee, I am Marty Kanner. I am testifying today on behalf of Consumers for Fair Competition (CFC), a coalition of small business interests, power marketers, consumer and investor owned utilities, small and large electric consumer representatives and environmentalists. Chairman Bliley has repeatedly called for putting consumers front and center in the restructuring debate, and the members of CFC want Congress to pass legislation that will enable electric consumers to realize the benefits of competition. As underscored by a recent letter sent to Congress by more than 100 organizations, which I have attached to

my testimony, legislative action is imperative to correct the significant failures in the wholesale electric market and create the open highway of commerce needed for state retail competition efforts to succeed.

As I have testified before, this is not an infant industry in which business success is decided by innovation, entrepreneurial prowess and efficiency. We are attempting to restructure an industry of government-sanctioned monopolies that control the vast majority of generation, transmission and distribution facilities and associated customer information. Despite the Energy Policy Act and other efforts to infuse competition in the wholesale market, the reality is that there is **not** robust competition in the market today:

- System constraints and market manipulation have caused wild price volatility and price spikes that—had retail consumers not been insulated by price caps—would have led to outrageous electric bills and an outcry for action;
- Large, vertically-integrated utilities have a chokehold on the transmission system and all users and uses of the grid don't operate under the same tariff;
- Many regional power markets are dominated by a single or small handful of players, that can dictate prices and shut out competitors;
- The continuing wave of utility mergers are likely to accelerate this consolidation; and
- Utilities continue to leverage ratepayer-provided funds and resources to enter new business lines through unregulated affiliates that compete unfairly with small and large businesses.

As CFC has previously testified before this subcommittee, Congress must pass legislation to achieve a market in which these structural flaws are remedied so that consumers have many choices, competitors are not unfairly disadvantaged, and competitive market forces prevent consumer abuse and market manipulation.

H.R. 2944, if enacted in its current form, would not create the vibrant competitive market that consumers want and need. In fact, it would be a step backward.

Transmission

The nation's transmission grid is the highway of commerce. Even in the states that have adopted retail competition, consumers won't be able to effectively choose among suppliers if those suppliers cannot gain access to the market. Despite the progress made in the Energy Policy Act of 1992, the transmission network remains a two-class system, with transmission owners granting themselves first-class service while competitors are relegated to the end of the line. All users of the transmission grid must operate under the same tariff and have the same tariff choices.

Today, each utility's transmission network, despite a certain amount of reliability coordination, is operated largely as if it were an isolated island. This unnecessarily constrains and contracts markets. By acting in their own self-interest, owners can:

- reserve the majority of transmission capacity for their own use (which use is not effectively subject to FERC comparability standards);
- hide retail and wholesale charges in bundled rates and create a lack of transparency in the transmission market;
- operate the system to favor its own (or affiliates') wholesale or retail marketing function,
- take actions ostensibly for reliability purposes—such as congestion management and emergency curtailment procedures—in a discriminatory and anti-competitive manner,
- impede the development of and sales by competing power suppliers; and
- fail to make transmission investments that would alleviate congestion and promote the competitive market.

Provisions in Section 101 of H.R. 2944 erode existing transmission access standards and drastically reduce the amount of transmission that would even be part of the interstate grid. A recent decision in the 8th Circuit has crippled FERC's vaunted "comparability" standard. Section 101 would codify this decision by granting the states exclusive jurisdiction over bundled transmission service. Such action effectively limits application of open access policies to the 10-15 percent of transmission capacity that are surplus to a utility's own needs.

The impact of this provision on bundled transmission service is compounded by subsection (h) which facilitates the reclassification of transmission facilities as distribution—outside the scope of comparability requirements. Such reclassification can also result in discriminatory cost-shifting to entities receiving service on these reclassified lines.

Combined, these provisions dramatically shrink the transmission network and cripple interstate commerce. It would be like allowing parts of the interstate highway system to be reclassified as county roads that then have toll gates erected. If

these provisions are not changed, even the most robust RTO provision would not create the open system needed for competitive electricity markets.

Unfortunately, H.R. 2944 does not advance effective RTOs.

CFC believes that control of the nation's transmission system must be transferred to truly independent bodies that encompass the broadest geographic regions and have strong authority to operate, plan, maintain and expand the transmission system. Such entities must provide for the functional separation of the monopoly transmission and market functions. It is imperative that all users of the system have equal, and non-discriminatory access to the nation's grid.

The provisions of section 103 do not break the utility stranglehold on the transmission system nor foster the open markets that must be achieved:

- *Utilities are allowed to structure RTOs to serve their own interests rather than having an independent referee promote RTOs based on the interests of the market.* Section 103 fosters a "take it or leave it" approach. While utilities are required to establish or join an RTO and the FERC is given standards by which to judge these filings, the Commission cannot require formation of or participation in an RTO if the filing fails to meet the standards. Thus, utilities could file inadequate RTOs and FERC is left with the choice of accepting "half a loaf" or rejecting the filing and retaining the flawed status quo.
- *The bill doesn't foster true independence.* By allowing 10 percent voting interests to pass the "independence" test, a small handful of utilities within an RTO can hold a majority of the voting interests. This is hardly a separation of the ownership and control of transmission and generation and creates a loophole that guts the underlying purpose of the RTO.
- *Bill encourages, small, numerous RTOs.* H.R. 2944 encourages smaller, more numerous RTOs that will encourage "pancaking" rates and increase costs for consumers.
- *RTOs would become an exclusive club.* The provision allows transmission owners to shut out new market entrants, end-users and transmission dependent utilities from the RTO process.
- *The RTOs responsibilities are limited—we cannot allow monopolists to set the rules of the market.* The provision allows RTOs that have no meaningful authority, simply administering rules and procedures established by the transmission owners. The provision fails to provide authority over associated generation that is essential for transmission regulation. Moreover, the bill is silent on which entity—the RTO or the transmission owner—will calculate available transmission capacity and reserve requirements and implement curtailment and reliability procedures.
- *Transmission incentives send the wrong signal.* Cost based pricing is the proper norm for monopoly services. We do not believe that incentive rates are needed or appropriate to induce formation of RTOs, eliminate rate pancaking, or minimize cost-shifting. The failure to invest in transmission has more to do with the strategic and financial value in sustaining transmission bottlenecks than the lack of "incentives". While congestion pricing can be used to reflect true transaction costs and encourage new investment, utilities should not be rewarded for providing an essential, monopoly service. Transmission incentives are not needed.

Failure to provide an open highway of commerce, in which all users operate under the same tariff and have the same tariff choices, will raise rates, frustrate competition and lead to the further balkanization of the system.

Market Concentration

In the electric generation market, market boundaries are determined largely by transmission constraints—physical limitations on transfer capabilities. Within these boundaries, it is common for an incumbent utility to own more than 40 percent of the generating capacity. At this level of concentration, economists recognize that the dominant firm can set and control prices above what would occur in a truly competitive market.

Despite a significant increase over the past few years in the construction of non-utility generation, such facilities still represent a comparatively small fraction of total generation. Moreover, potential developers of such facilities often face a diverse set of entry barriers. For example, incumbent utilities displace competitors in the queue to connect new power plants to the grid. They also own the prime sites for future plant location (often adjacent to existing plants). In addition, in many states, only utilities themselves can request and receive the necessary regulatory permits. Even if new, independent plants can be built, it will be years—and there will need to be considerable growth in demand—before competitive suppliers will break the lock of the dominant player and markets will begin to operate competitively.

CFC supports the provisions of the DeLay-Markey bill of last Congress, which grants FERC affirmative authority to investigate and remedy undue concentration, as an effective means for addressing this problem. Alternately, Mr. Chairman, your state of Texas adopted provisions that provide a workable model for federal legislation. We would encourage you to provide consumers throughout the nation the same assurances of competitive generation markets that Texans will enjoy.

In addition, Congress must eliminate discriminatory standards for interconnection with the grid. We cannot allow utilities to advantage their own generation projects to the detriment of new market entrants.

Mergers

The various procedural limitations on merger review established by H.R. 2944 effectively eliminate meaningful review.

There are certainly potential utility mergers that do not warrant timely and extensive review. However, for many mergers, the time limits and elimination of hearings and cross-examination will severely limit the ability to analyze the competitive impact of the proposed merger. While there are time limits under the anti-trust laws in merger reviews, I would highlight that those same laws have robust data filing and discovery requirements.

We would urge you to delete the procedural limits in H.R. 2944. If the merger review process is to be truncated, then data filing and discovery requirements analogous to that which exists under the anti-trust laws must be established.

Affiliate Transactions

By straddling regulated and unregulated markets, utilities can cross-subsidized their competitive, unregulated activities with revenues and resources provided by captive ratepayers. Not only do such actions harm consumers, they harm the countless small and large businesses that the utilities unfairly compete against.

The information disclosure and consumer privacy provisions of H.R. 2944 are important steps in addressing some of the underlying problems in affiliate transactions. However, more is needed. While state commissions can review and regulate the practices of utility affiliates providing energy services, they are unlikely—or often unable—to review the activities of utility affiliates in energy related enterprises targeting residential and commercial markets for electrical, mechanical, air conditioning and heating and fuel supply markets. State Commissions already act on behalf of consumers. Now they need the direction and authority to act on behalf of existing competitors in a deregulated retail energy market.

Congress recognized the need to prevent anti-competitive cross-subsidization in the 1996 Telecommunications Act. Congress should not set a lower standard of fair competition for the energy market than it did for the telecommunications market. CFC urges Congress to prohibit cross-subsidization, adopt model structural and behavioral standards for state commissions and establish a cause of action for abusive affiliate practices. We believe the limitation on books and records under the PUHCA provisions are a step in the wrong direction.

Conclusion

The current system is not working, and action is needed to correct market deficiencies and promote competition.

Congress must make a clear choice: advance the interests of monopolists, or the interests of consumers and competition. These are not issues that can be balanced or compromised. In order to achieve the benefits of competition, we must eliminate the anti-competitive vestiges of the old, regulatory system.

Mr. Chairman, we appreciate your openness to improving amendments and look forward to working with you and the members of the Committee to develop a bill that advances a competitive electric marketplace.

Mr. BARTON. Thank you, Mr. Kanner.

We would now like to hear from Mr. Richard Cowart, who is the director of the Regulatory Assistance Project.

Mr. Cowart?

STATEMENT OF RICHARD H. COWART

Mr. COWART. Thank you, Mr. Chairman.

I guess I should emphasize that I speak today as someone who for 12 years sat as the Chair of a State Public Utility Commission, and my views are my own.

As is obvious to the members of the committee, the subject of electric restructuring is no longer a theoretical one. The States have clearly been the laboratories of democracy in this transformation, and the good news now is that Congress can learn from what has been going on throughout the Nation.

A review of this bill reveals that much has been learned from the policy debates and experiences of the States.

Provisions in the bill on consumer protection, electric product disclosure, net metering, and a number of the transmission and reliability provisions are commendable. In other areas, though, it seems that key lessons from recent experiences around the country are not being dealt with in Congress.

In particular, the draft bill does not adequately address the challenges we now face in maintaining environmental quality, universal service, and electric system reliability. And in my short time with you today I am going to focus on reliability.

We know that this is the most important goal of the American electric system. Customer polls consistently reveal that keeping the lights on reliably is the top priority that people have for the electric system, and it is the No. 1 concern that they have about industry restructuring.

In recent months, it has become clear that the reliability of the Nation's electric system is under great strain. Outages, power warnings, price spikes, rolling brownouts—I think you know the litany of events that have occurred in all regions of the country over the past 2 or 3 years, and particularly during the summer peak periods.

The North American Electric Reliability Council, which likes to speak quietly on such things, is starting to warn that we face a real reliability problem, and I heard Mr. Nevius say this morning that we need reliability legislation now.

The common response to the events that we are discussing here has been a call for more construction of more energy supply facilities—90,000 megawatts, 100,000 megawatts, 120,000 megawatts of new generation is often called for—along with the accompanying gas pipeline capacity and electric transmission capacity to serve this growth in output and throughput.

But there really are three elements to the equation, and the bill only deals with two of them. The three elements are: generation, transmission, and end uses. We need to focus for a moment on the end use issues.

The reliability problem that we now face is, in large measure, the result of rapid load growth over the past decade, coupled with a serious falling off in efficiency and demand side management measures by the Nation's utilities.

According to the EIA, electric consumption grew by 31 percent over the past decade. In the critical summer peak period, growth has even been more dramatic—a 56,000 megawatt increase between 1993 and 1997, alone.

This is the electrical equivalent of adding the entire six-State region of New England to the Nation's peak demand every 18 months, and that process is continuing.

Unfortunately, while this demand has been rising, utilities have been dramatically reducing their investments and their achieve-

ments in cost-effective energy efficiency and demand side management programs.

And we should pause for a moment to remind ourselves that these utility efficiency programs have, in fact, been very successful.

In the early 1990's, energy savings were rising annually at double-digit rates, costs of power reduction averaged 2.1 cents per kilowatt hour, and peak load reductions of up to 29,000 megawatts were attained.

But with the advent of competition all this has turned down sharply. Total utility spending on demand side management and achievements in this area have dropped in half, and the achievements that were expected to be attained by now have also been dropped in half.

Utilities in 1993 expected that we would be now able to clip our peak demand by 55,000 megawatts. That has been reduced to 25,000, leaving an efficiency gap of about 30,000 megawatts.

Just imagine for a moment what an extra 30,000 megawatts of non-polluting——

Mr. BARTON. Mr. Cowart, would you suspend? We are not going to take this away from your time. I would just make an announcement to the subcommittee. I am told we have three 15-minute votes, and I count three more witnesses after Mr. Cowart at 6 minutes each. That is 18 minutes.

So at the conclusion of Mr. Cowart's testimony we are just going to put a little firewall right there between Mr. Cowart and Mr. Smith and take a lunch break and we will reconvene at 1:30. But we are going to finish with Mr. Cowart, take a break, come back at 1:30. Every member of the audience has to be back in the same seat at 1:30, and then we will hear from Mr. Smith, Mr. Casten, and Mr. Segal.

Continue, Mr. Cowart.

Mr. COWART. All right. Thank you.

Imagine what an extra 30,000 megawatts of non-polluting capacity could have achieved to forestall the blackouts and power outages that we have been seeing over the past couple of summers.

The potential for energy efficiency investments in this country is by no means exhausted, and the good news is that it would save a lot of money, it would leave a lot of money in the pockets of American households and at the bottom lines of American businesses.

There are a number of important provisions in this bill to strengthen the reliability of the electric grid, but when you are trying to keep up the water level in a big reservoir, you might need some bigger pumps and you might need some bigger pipes, but it is also smart to see if the water on the other end is just leaking into a hole in the ground.

We need to go out and work on energy efficiency, Mr. Chairman, as part of the restructuring of the electric industry.

Now, the good news, in conclusion, is that the States have been working on these issues, and there are good models out there, both for the provision of energy efficiency services and also for the provision of renewable energy services to American consumers.

I would commend the committee's attention to the work the States have been doing in this area, and I would recommend that you add provisions to support those measures to this legislation.

[The prepared statement of Richard H. Cowart follows:]

RESTRUCTURING, RELIABILITY, AND THE PUBLIC GOOD

Testimony of Richard H. Cowart
Before the Subcommittee on Energy and Power
Of the Committee on Commerce,
U.S. House of representatives

October 6, 1999

I. Introduction

Mr. Chairman and members of the Subcommittee, I appreciate the opportunity to speak before you on the transition to competition in the electric industry. This is one of the most complex policy issues facing the nation today: we seek to improve the efficiency of a key industry that is deeply affected with a public interest, an industry that has disproportionate environmental impacts, but which is also critical to the economic well-being of virtually every household and business in the nation. My message today is straightforward -- as we reform our nation's electric system to capture the benefits of competition, we must secure, and if possible, enhance, the public benefits that have been provided by the industry's unique structure and regulatory traditions. The means to secure these public objectives can, and should, be designed into any new regulatory structures from the outset — before dramatic changes completely unravel the gains this industry has made.

I am Richard Cowart, Director of the Regulatory Assistance Project, a nonprofit organization whose principal mission is to provide technical and policy assistance to the nation's public utility regulatory commissions. I also serve as Executive Director of the National Council on Competition and the Electric Industry, the leading national association of state and federal officials governmental decision-makers who have, within their jurisdictions, significant responsibility for power sector reform. The National Council has conducted research, hosted forums, and provided technical briefings all across the nation on the issues that are now before your committee. For most of the past 13 years, moreover, I had the privilege to serve as Chair of the Vermont Public Board, supervising utility services in my state, and my testimony today is chiefly based upon that experience. However, the opinions expressed here are entirely my own, and I am not today appearing for any of these organizations.

The topic of electric industry restructuring is very broad, and the draft of H. R. 2944 addresses many issues, but I understand that I've been invited today to focus on utility programs and policies that have long advanced the interests of consumers and the public good. As the drafters of the Federal Power Act and numerous state enabling statutes were well aware, the electric industry has long been recognized as one uniquely affected with a public interest. Both regulatory traditions and public expectations underscore this fact.

Restructuring policy debates have, of course, many moving parts, but they can largely be summarized as focusing on a trio of challenges: allocating and recovering stranded costs; controlling market power; and preserving stranded consumer benefits. The public debates in

many states, including my own, have focused a great deal of attention on the stranded cost leg of this tripod. But I strongly suspect that a decade from now the success of our efforts will be measured not so much by our approach to stranded cost recovery — but rather by how well we have dealt with the other two challenges. My focus today is on "stranded benefits"— the electric industry's historic commitments and investments that benefit consumers, the environment and the nation's energy future, but which are threatened in the movement to a purely competitive electric system.

These are not esoteric issues or the fringe positions of special interest groups. By extremely large majorities, Americans in all regions of the country support utility reforms that will continue to provide reliable universal service, lower bills, and a cleaner environment. In a unanimously-adopted resolution, the nation's utility regulators stated in 1994, "a fundamental responsibility of state and federal electric utility regulators in this transition period is to assure that vital public interests and established public benefits will be preserved in any restructuring of the electric utility industry."[2] NARUC later explicitly urged "Congress, as it considers legislation to restructure the nation's electric industry, to include in such legislation workable mechanisms to support State and utility public benefits programs such as energy-efficiency, renewable energy technologies, research and development and low-income assistance..."[3] Legislatures and Governors from both parties in all regions of the nation have endorsed measures to advance these goals.

Despite widespread support for the public purpose traditions of the utility industry, it is apparent that those purposes are not well maintained in a purely competitive generation system. The commercial and legal restructuring going on today is profoundly undercutting the ability of the nations utility system to meet those traditional obligations In this context, Congress has the responsibility, as part of any comprehensive restructuring legislation, to address the challenges that restructuring poses in the areas of reliability, consumer protection, universal service, and environmental quality. H.R. 2944, as now drafted, does not yet adequately address those important issues.

II. Threats to Reliability and the Promise of Efficiency

The reliability of power supply is perhaps the most important goal of the American electric system. Customer polls consistently reveal that "keeping the lights on" reliably is the top priority among goals for the electric system, and is the number one concern of the public about industry restructuring. While competition in electric generation need not degrade the reliability of the electric grid, unfortunately it appears that reliability is now being undermined, and could be threatened further without changes in current trends. A major contributor to this situation is the utilities' abandonment of well-established energy efficiency programs in anticipation of retail electric competition. Dramatic cuts in utility efficiency and load management programs since 1994 have led to power shortages, overloaded transmission and distribution systems, blackouts, voltage reductions, and price spikes.

Why should this be so? It's useful to begin with an observation made by a power marketer at a recent conference, "When prospective customers ask me about reliability, I tell them that so long as they are connected to the grid, their reliability will be exactly the same as their neighbors, no matter who they buy their power from." This remark reminds us of a critical physical fact: electric system reliability is, in many respects, a classic public good. By the laws of physics, the essential attributes of adequacy, voltage, and frequency are available to all interconnected users simultaneously. Like the textbook examples of lighthouses and national defense, most aspects of electric reliability are provided to everyone or no one, so it's necessary to share their costs broadly. Public rules, imposed by governments, utilities, reliability councils or power pools, will determine the costs of reliability measures and the means of paying for them. In this environment, the cost of degraded reliability is a cost that everyone will share, while low-cost reliability enhancements will provide benefits to customers throughout a region.

Reliability — A Growing Concern

In recent months, it has become clear that the reliability of the nation's electric system is under great strain. Outages, power warnings, blackouts, rolling brownouts, and price spikes have arisen at a rate not seen in the United States for decades. In August 1996, a transmission failure during a period of peak demand led to a multi-state blackout in the West, interrupting 30,000

MW of load to 7.5 million customers, some for as long as 9 hours. By some estimates, the cost of this outage in California alone approached $1 billion.[4]

In August of 1998, the New England ISO issued a system wide power watch; New York Power Pool members were asked to request conservation measures from customers; in the Pennsylvania-New Jersey-Maryland Power Pool, prices reached $1000/MWH, 50 times their usual level; in the Midwest, Detroit Edison and Consumers Energy asked customers to cut back, while UtiliCorp United, Kansas City Power & Light and Interstate Power all ordered interruptions for interruptible customers. In California, San Diego Gas & Electric set a new system peak and called for conservation measures, while the California ISO declared a Stage 2 Emergency when operating reserves fell below 5%.

These critical peaking problems continued into 1999. In New York City, on one of the hottest days of the year, a power cable short-circuited, leaving 200,000 homes in the Washington Heights section of Manhattan powerless for 18 hours, the worst blackout to hit the city in 22 years. In New Orleans, power-plant failures led to blackouts that disrupted service for more than 500,000 customers. In Chicago, repeated outages blacked out the downtown Loop, leaving 2300 business in the dark, and cut off power to as many as 100,000 homes. These outages, as dramatic as they are, are just the most obvious symptoms of increased peak demands and lowered reserve margins throughout the nation. In 1990 there was a 22 percent cushion of extra power available for emergency use in the United States. That figure fell to 16 percent in 1997, and according to the Edison Electric Institute will drop to 10 percent by 2007, if consumption continues to grow at current rates.[5]

A common response to these events has been a call for more construction of energy supply facilities: a huge increase in power plant capacity, supported by expanded gas pipeline capacity, and incentives for the construction of new electric transmission lines. Many market participants have called for 90,000 to 100,000 MW or more of new generation capacity over the next 7 to 10 years, together with the pipeline and transmission system improvements needed to support those plants.[6] Those facilities, and their operating and maintenance costs, will ultimately cost American families and businesses hundreds of billions of dollars in their electric bills over the next twenty-five years.

However, a closer look at all of the underlying causes of the current capacity and reliability problems reveals a more promising policy option: a substantial part of the nation's existing and projected power supply needs could be met more reliably and at lower cost through energy efficiency programs aimed at reducing peak demands, and relieving the strain on overloaded transmission and distribution systems. Federal electric restructuring legislation should include workable mechanisms to identify and support low-cost efficiency solutions to reliability challenges.

Roots of the problem: Demand growth up, efficiency and load management down

The reliability problem that we now face is in large measure the result of rapid load growth over the past decade, coupled with a serious falling-off in efficiency and demand management investments by the nation's utilities. According to the Energy Information Administration (EIA), annual electric consumption grew by 31% between 1988 and 1998. Load growth has been even more dramatic in the critical summer peak period: between 1993 and 1997 alone, summer peak loads grew by 56,000 MW. To put that in perspective, this is the electrical equivalent of adding the peak load of the entire six-state New England region to the nation's electric demand every 18 months.[7]

Unfortunately, as the economic expansion has driven electrical demand up, utilities have also been dramatically reducing their investments and achievements in cost-effective energy efficiency and demand management programs:

- Total utility DSM spending has declined by about 50% since 1993. According to the EIA, utility spending for all DSM (efficiency and load management) totaled $2.7 Billion in 1993; EIA at the time projected an increase is DSM spending to about $3.5 Billion by 1998. Instead, spending has dropped to $1.5 Billion, a decline of 45% in four years, and a reduction of 57% as compared to the trend line of 1991-93.[8]

• The abandonment of utility-sponsored DSM programs between 1994 and 1999 has dramatically reduced the contribution such programs could have made to meeting both energy needs and peak demands last summer. DSM-related peak load reductions totaled more than 20,000 MW by 1993, which the utilities then projected would rise to 55,000 MW by 1998. However, only 25,000 MW of peak reduction was achieved in that year. Thus, there now appears to be an "efficiency gap" of approximately 30,000 MW of lost peak reduction due to the rapid abandonment of these programs since 1994. Incremental energy savings from utility energy efficiency programs (additional savings relative to savings achieved in the prior year) have also been cut in half, dropping from 8.6 billion kWh in 1994 to 4.3 billion kWh in 1996.

The abandonment of energy efficiency programs by utilities is widespread, and it is occurring despite the proven track record of these investments. Over the past decade, we have learned two important facts about energy efficiency, mostly through the implementation of utility-sponsored Demand-Side Management (DSM) programs. First, we have learned that the potential for cost-effective savings from accelerated investments in energy efficiency is very large. And second, there is a growing body of empirical evidence that there are significant market barriers to the commercial deployment of those investments in the absence of public support and coordinated delivery mechanisms. Those market barriers will not be erased by the move to retail competition in electric generation, and will continue to stand in the way of a more efficient economy unless utility and public efficiency programs are maintained.

Individual DSM programs vary in their size and cost-effectiveness, but the overall results of utility DSM programs over the past decade have been remarkable. Even in a period of start-up, experimentation, and institutional development, utility-sponsored DSM programs quickly lowered the nation's summer peak load by more than 25,000 MW, and delivered energy savings to utility systems at a cost to the utilities of about 2.1 cents per kwh.[9] And the national potential for efficiency savings is by no means exhausted. Moderate estimates by experts at the nation's energy laboratories are that by 2010, efficiency programs could reduce the nation's overall electric consumption by 15%, saving more than $23 Billion in the process.[10]

The proven advantages of efficiency technologies are being lost as generation plants move out of the ownership of vertically-integrated utilities serving retail loads under direct state jurisdiction and into competitive regional markets not subject to the principles of integrated resource planning or the oversight of the states' public utility commissions. As a result, the reliability of the electric system is compromised, and electric service is more expensive and more polluting than it should be. Efficiency technologies can be the most modular, most dispersed, least expensive and least environmentally harmful means of meeting a critical fraction of our nation's growing electric demand. Comprehensive electricity restructuring legislation should include support for the continued deployment of these investments for reliability, economic, and environmental reasons.

III. Portfolio Diversity and Renewable Energy

Under traditional regulation, most electric utilities have been able to assemble resource portfolios that give their customers the benefits of cleaner energy, long term investments, risk management and resource diversity. To a certain extent, these benefits are the result of economic choices that can be dealt with by individual customers, brokers and producers in a market system. But they also raise important questions for the nation as a whole.

We have learned the hard way that the nation's economic well being can be put at risk by rapid spikes in world energy prices. Future dislocations could result from newly understood international environmental problems, fossil-fuel supply interruptions, or operating problems at nuclear power plants. Moreover, renewable energy technologies represent a huge international market for the next century. If American industries are to participate in that future, technological and operating gains must be captured by American firms now and over the next decade.

History teaches us that a policy of prudent energy portfolio diversification is a form of national economic and environmental insurance that is well worth purchasing. It is not sufficient simply to assert that price spikes and supply disruptions are risks that markets will account for and that governments can ignore. It is prudent, sensible and in the public interest to ensure that our nation's portfolio of well-developed energy choices, including renewable resources, is not undermined by our choice of structures for the electric industry.

IV. Universal Service

As we seek to restructure a major institution in a democratic society, fairness is an important consideration. Utilities and their investors have been understandably quick to assert that historic commitments made as part of the regulatory bargain should be honored in the transition to a new structure. There is merit to this claim, but equally there is merit to the claims of customers, including residential, small business and low income customers, who have also supported the current industry structure and who have benefitted from the commitments of the past. Among those benefits are low income assistance programs, disconnection moratoria, customer service protections, and equal access to the benefits of the utility power portfolio.

Low income households typically devote a much larger percentage of their total household income (roughly 15%) to energy bills than the rest of us (approximately 3.5%). High heating and cooling bills are a major problem for low-income and elderly customers, often with very serious health and safety consequences. Recognizing that affordable electric service is essential to participation in modern society, the franchise system has traditionally provided assistance to households in need. Annually, across the nation more than two million residential customers benefit from bill assistance and disconnection protections.

We must find ways to ensure affordable access to electricity, and to ensure that the benefits of competition are available to utility customers of all types and sizes, not just to those with exceptional market power.

V. Workable mechanisms for federal legislation: The Renewable Portfolio Standard and the System Benefits Trust

As the testimony above makes clear, the nation's electric companies have long had both the responsibility and the means to provide energy efficiency programs, renewable energy supplies, and affordable, universal service to low-income households. Unfortunately, under the pressures of increasing competition and corporate restructuring, utilities' investments for these public purposes have dropped dramatically. The chart below summarizes these trends:

SYSTEM BENEFITS TRENDS

	1994	1998	% Change
Renewables	kWh 66 billion	kWh 49 billion	-25%
DSM	$2.7 billion	$1.5 billion	-45%
	1993	1995	
IOU R&D	$650 million	$500 million	-23%
	1985	1997	
LIHEAP	$1.7 billion	$1.03 billion	-41%
	1990	1996	
Weatherization	$152 million	$91 million	-40%

These trends should not come as a surprise. For example, a vertically-integrated utility subject to cost-of-service regulation can be expected to invest in demand-reducing technology for the benefit of its customers; but a competitive generator or power marketer has almost no interest in those solutions. Historically, franchise utilities in a power pool, each with a secure customer base and the promise of cost recovery through rate regulation, could each go along with the complex give-and-take that made it possible for them all to provide power reliably. But now, those providers are all potential competitors, and each has an incentive to minimize its contribution to overall system reliability, and to maximize the gain on sales to the pool during peak periods. These problems can be addressed through effective, independent system management, but the cost to the public and the cost to the environment will be much lower if

energy efficiency investments are part of the equation. Since power pools and power markets transcend state borders, reliability problems often affect customers in multiple states whether or not they are responsible for the shortage. Power pools and system operators routinely impose expensive reserve requirements, ancillary service requirements, and other costly reliability measures on consumers throughout a region. Energy efficiency investments will often be a less expensive and more robust answer to these problems; there is therefore an appropriate federal role in advancing efficiency programs as part of restructuring legislation.

A. Meeting Public Goals: The Electric System Benefits Trust

Restructuring offers a unique opportunity to implement viable, cost-effective programs that promise a clean, sustainable, affordable energy future for all Americans. As noted above, electric utilities across the United States have historically made highly productive investments in energy efficiency, renewable energy, low-income service, and long-term research and development. These are not new expenditures. In recent years, approximately $6 billion per year has been included in utility rates nationwide to support public purpose programs.

As the restructuring debate moves to Congress, it is essential that we develop effective mechanisms to deliver these important benefits. These mechanisms should not distort emerging competitive markets in electricity, nor should they erode states' traditional responsibilities for ensuring that electricity-related public benefits are widely and appropriately shared. An efficient federal mechanism to support state action in these areas is the System Benefits Trust (SBT). The SBT is a competitively-neutral means of supporting utility services at the state level, and within the utility system. It encourages state initiative and avoids any new demands on the federal treasury or any mandates for state or utility spending. The objective is to reward states for their leadership and responsibility in delivering public benefits associated with electricity service.

1. The Proposal

Under this proposal, Congress would create a national "Electric System Benefits Trust" to inspire and support state programs for energy efficiency, renewable energy technologies, R&D, and low-income assistance. The trust would be supported by a broad-based, competitively neutral, and very small national "system benefits charge" levied as an access charge on all interconnected generation at the busbar or system operations level. The Trust's funds would be used to match funds raised by the states for the same purposes. This program should be *in addition to* other federal initiatives (e.g., a renewables portfolio standard, continued low-income energy assistance funding, research at the national labs, and appliance efficiency standards). It does not replace those programs. It supports continuation of utility-sponsored programs historically managed at the state level.

While electric industry public purposes programs have historically been supported at the state level, these programs advance important national goals, such as resource diversity, national security of energy supplies, environmental protection, and economic development. In doing so they provide benefits to the entire nation.

2. Design Principles

To be most effective, national systems benefits programs should be designed to meet the following criteria:

- **Promote Competition.** System benefits charges should be competitively neutral, non-bypassable, and small in proportion to total system revenues.

- **Stay Within the Utility System.** Receipts raised through system benefits charges will be paid by utility customers for utility-related purposes. They are included in utility rates today, and should be considered as rate elements in the future. As with transmission rates, reserve requirements, and environmental compliance costs, they are utility system program costs, not general governmental taxes or revenues.

- **Support State Initiatives.** Federally authorized access charges are not intended to create new federal programs--but, rather, to inspire and support state-level programs in the national interest. Funds raised at the broad generation or transmission level should be distributed directly to states and their agents for program administration.

- **Accountability to Rate-Setting Authorities.** Following general enabling legislation, oversight of system benefit charges should rest with FERC and state utility commissions, employing rate-setting and rule-making procedures similar to those used to implement telecommunications public purpose programs (e.g., the use of Joint Boards, independent fiscal agents, and rate level adjustments to "true-up" accounts over time).

3. Program Elements

An effective System Benefits Trust could be built on the following basic program elements:

(a) Each state would determine whether, and to what degree, it would sponsor eligible public purpose programs: R&D, renewables, energy efficiency, and low-income/affordability support. Eligibility and program design issues should be handled by a joint state-federal oversight board.

(b) Each year, a rate-setting entity (preferably a federal-state joint board) would calculate the national access charge necessary to match the level of state funds being raised for eligible programs. Transmission owners or ISOs would collect this charge on a uniform national basis on generators at the busbar, or from transmission users as a component of transmission rates. In either event, the charge should be volumetric and non-pancaked, to avoid any competitive distortion to transmission prices. This fund would be designed to "zero-out each year, with small carry-forwards or true-ups as necessary to match eligible state funds without building up a significant fund balance.

(c) The national systems benefits charge could be capped at a predetermined level. (For estimation purposes, each 1 mill per kWh would raise about $2.9 billion nationally.) A 1:1 state-national match could be used at the outset, but this ratio could change.

(d) National system benefits funds would be collected by transmission companies or ISOs and paid into the Electric System Benefits Trust – a pool administered by an independent, non-governmental fiscal agent, akin to the National Exchange Carrier Association, the fiscal agent that handles the exchange of payments among the nation's toll and local telephone companies for the use of each others' switches and networks. Electric system benefits charges are costs for utility services, and would be treated as utility system revenues, not general governmental receipts.

(e) The fiscal agent would distribute eligible funds to program agents in each state as designated by each state's enabling legislation or regulatory commission—likely the same distribution utilities, ESCOs, or other agents that administer the programs set up by the states in the first place. No federal bureaucracy is required; other than the fiscal agent, no new program administrators are necessary.

B. <u>The Renewable Energy Portfolio Standard</u>

The Renewable Energy Portfolio Standard (RPS) has emerged as the leading proposal for capturing the environmental and diversity benefits of renewable energy technologies in an increasingly competitive marketplace. The RPS is a proposed national performance standard that would ensure a small but steadily growing proportion of renewable energy in the mix provided by all electricity suppliers. All federal RPS proposals also include a renewable energy credit trading mechanism.

Renewable credit trading is analogous to the sulfur allowance trading system that has worked so well in reducing the cost complying with the acid rain title of the Clean Air Act. Renewable energy generators are issued credits for each unit of renewable energy generated. Electricity suppliers then can choose either to generate or buy sufficient credits to demonstrate compliance with the renewable energy standard. They can buy credits when they buy renewable kilowatt hours, or from other generators or marketers with surplus credits, or from a secondary credit trading market.

By creating a market for renewable energy credits, the RPS will stimulate investment in renewables in an environment where energy producers must keep their energy products competitively priced in order to attract customers. More importantly, the RPS reduces renewable energy costs to help integrate these needed technologies into an increasingly competitive market by:

- Providing assurance of an expanding renewables market, enabling manufacturers and developers to make the investments needed to achieve economies of scale in manufacturing, installation, operation and maintenance.
- Requiring renewable energy projects and technologies to compete against each other to meet the standard at the lowest cost.
- Creating an incentive to develop renewables wherever they are most cost-effective. If marketers can buy credits from renewables anywhere in the country, developers can site them where the resources are the best and not have to build or pay for long distance transmission.
- Reducing transaction costs associated with suppliers having to negotiate contracts with many small renewable energy projects.

The RPS is simple to administer, requiring only issuing of credits to generators and counting credits of suppliers. No one picks winners and losers, either among renewable energy technologies or among renewable energy projects. The market decides which renewable energy technologies and projects get built and where.

A number of RPS proposals have been introduced in Congress, ranging from 3% of sales by 2010 to 10% of sales by 2010 and 20% by 2020. Some observers have asked whether the RPS proposals at the high end of the range are feasible. Many studies have shown that the United States has a vast renewable energy potential, equal in theory to many times current electricity use. The important question, then, is not whether standards of 10% or 20% of electricity sales are technically feasible, but how much would they cost. Several studies have looked at this question:

- The Energy Information Administration calculated that an RPS of 10% by 2010 would gradually increase electricity prices compared to no RPS. In 2010, the typical (500kWh per month non-electric heat) residential customer would pay about $1.50 (4%) more than without an RPS. But with the RPS, prices would still be 17% lower in 2010 than they were in 1996. Moreover, the added renewables would create enough competition for natural gas to restrain gas price increases. According to the EIA study, lower gas prices and conservation savings would more than offset the higher electricity prices.
- The Department of Energy Office of Policy's analysis of the Administration's 7.5% by 2010 RPS found that the typical residential customer would pay about 80 cents more per month in 2010 than without an RPS.
- The Union of Concerned Scientists' analysis of an RPS that would grow to 10% by 2010 and 20% by 2020 found that electricity bills for the typical residential customer would be 56 cents per month more in 2010 and $1.33 per month more in 2020 than without an RPS.

- Importantly, in each case, a national RPS has a small impact on electric bills, but electricity prices still decline significantly in every case. The savings resulting from competition and from accelerated efficiency investments more than offset the cost of renewable supplies. The RPS simply invests a fraction of these national electricity savings in diversifying our electricity supply with low impact domestic energy resources.

The RPS would deliver important environmental and economic development benefits. According to the EIA's analysis, for example, the 10% RPS could reduce nitrogen oxide emissions, which contribute to smog, by almost half a million tons, or by 8% from projected levels. According to the DOE, biomass and wind development from the RPS could mean over $1 billion per year in new income for farmers and tens of thousands of new jobs.

Is the price of an RPS reasonable? Survey after survey has shown that Americans want cleaner and renewable energy sources, and that they are willing to pay more for them. A recent survey for the Sustainable Energy Coalition found that 79% of voters support an RPS of 10%, vs. 17% who oppose. By 59% to 37%, the sample also supported a public benefit trust at levels two to three times higher than the level proposed by the Administration.

Some have asked, if consumers are willing to pay more for renewables, why not just leave developing renewables to the so-called "green market?" Over the long-run, many analysts believe that green customer demand could be significant. But there are many barriers to such markets, including; a lack of information, very high marketing and transaction costs, inertia, and the fact that two-thirds of electricity is bought by commercial and industrial customers who are likely to be much more sensitive to price than to the environmental characteristics of their energy supply.

Moreover, when given a choice, people have consistently said that they prefer that everyone pay to help develop new, cleaner technology, rather than relying only on volunteers. A Texas Utilities deliberative poll found that 79% of participants preferred that everyone pay a small amount for renewables, versus only 17% relying only on green markets.

Those results underlie why Texas recently became the latest state to adopt an RPS. The Texas restructuring bill, signed by Governor George W. Bush, created the largest single market for new renewables in the country, 2000 MW by 2010. At least six other states have enacted Renewables Portfolio Standards as part of restructuring. Three additional states have enacted minimum renewable energy requirements outside of restructuring, while to date, ten states have enacted public benefits funds as part of their restructuring initiatives.

VI. Conclusion:

In electric industry restructuring, legislators and regulators face the challenge of harnessing the benefits of competition without sacrificing the values long served by the franchise system and its regulatory traditions. We also seek to promote the national good while respecting the expertise, initiative and unique circumstances of the several states. At least 15 out of the 22 states that have enacted restructuring legislation to date have included either a renewables portfolio standard, a system benefits trust, or both in their restructuring plans. However, the benefits of pool-wide reliability, of reducing air emissions, of diversifying our fuel supplies, of enhancing out energy security, and of supporting American-made technologies and energy are national benefits that need national support. State-by-state programs will also come under increasing pressure to "race to the bottom." We must not rely on a handful of states or on volunteers to provide these national benefits.

Together, the RPS and SBT help to ensure that the new electricity market is one in which all Americans have affordable and reliable access, where renewable energy sources are a important component, and where investments in energy efficiency, can deliver significant economic and environmental savings to the nation.

ENDNOTES

1. A complete list of the National Council's research reports and publications is attached as Appendix 1.

2. NARUC, "Resolution on Competition, the Public Interest, and Potentially Stranded Benefits (Adopted November 16, 1994)

3. NARUC, "Resolution Endorsing Federal Legislative Provisions to Preserve and Promote Public Benefits Programs in the Nation's Electric Industry" (Adopted November 12, 1997)

4. Electric Power Research Institute, "Electricity Policy Roadmap," July 1999, # p. 22.

5. For further detail and observations on the 1999 outages, see Pam Belluck and David Barboza, "After Summer's Power Failures, Concerns About Large Utilities," New York Times, September 13, 1999.

6. See, e.g., "Nationwide Capacity Shortage by 2007?", Electricity Daily, June 4, 1999; and Energy Insight, "The Outlook for Power in the US--1998".

7. Summer peak for the six-state New England region has totaled approximately 20,000 MW in recent years.

8. A look at the 15 largest utility programs confirms this trend. Utility DSM spending has declined by about 50% at those utilities since 1993. A modest fraction of that spending has been restored by public benefits programs in a few states. (Chuck Goldman, Energy Analysis Dept, Lawrence Berkeley Lab, April 22, 1999)

9. This rises to about 2.9 cents, taking into account the time value of the investments made.

10. This is the conclusion of the "5 Labs Study", prepared by experts from five National Energy Laboratories.

Mr. BARTON. Thank you, Mr. Cowart.

The subcommittee stands in recess until 1:30.

[Brief recess.]

Mr. BARTON. We are going to go ahead and start. We had a malfunction of the House automatic teller machine, so there was a move to record the rule on health care by actual old-fashioned roll call vote, and, unfortunately, I am a "B," and before I knew about it they were past me, so I had to wait. I apologize.

Mr. SAWYER. Mr. Chairman, is this an electric reliability problem?

Mr. BARTON. It has been pointed out that there was a transmission access problem.

Actually, what happened, Mr. Barcia got a new voting card today. Our members are given these electronic voting cards. They put his name in it as Arcia, not Barcia. So when he recorded his vote, the electronics of the machine tried to find Arcia and went crazy because there is no Arcia, to it melted down the system, looping, trying to put the "no" vote of Arcia where there was no person. So they have corrected that problem.

Mr. Smith, your testimony is in the record in its entirety, and we recognize you for 6 minutes. I know it will surprise some of the audience, but you were my witness, which has got to be something of a first for me, having a representative of Public Citizen testify at my request.

Welcome.

STATEMENT OF TOM SMITH

Mr. SMITH. Mr. Chairman, I am honored. And thank you very much for your invitation. I am proud to be here.

I run Public Citizen's Texas office. As you know, we are a national nonprofit consumer organization, founded over 25 years ago now by Ralph Nader, and we are here today to talk about our concerns about electric utility deregulation.

Before I begin, I would like to say thank you to you, Mr. Chairman, and other members of this committee because there are a number of provisions in this bill that we recognize as being here because people like myself or others in the environmental community have asked for them—your disclosure section, the net metering section, your privacy and slamming and cramming sections, and, although we do not think they go far enough, the renewable sections that begin to encourage it through extensions of various tax credits.

I have basically five themes I want to talk with you about today. And let me begin by saying, for those of us in Texas and around the Nation who are looking at electric utility deregulation, the test is really who is going to benefit. Is Bubba going to benefit, or is it the big boys?

And what we see today is that there is not enough in this bill for Bubba to really benefit yet, and it seems to us it is kind of like crossing the stream. You have gotten about three steps out into the middle of the stream and the path is not clear to the dry bank on the other side, and if we do not get some more stones in the middle of that stream, we are all going to get wet and wish we would never have started to cross.

And so what I would like to do today is visit with you about some of those other stones that we think we can put in the stream that will get us to a place that may be better for us all.

First, let me go through the five or six big themes I want to talk about, and then I will come back and hit them in greater depth.

The first is, as you have heard across the table today, there is a lot of interest in aggregation. We think the most cost-effective way to serve the average residential consumer is through opt-out aggregation like they have in Ohio and Massachusetts, where a group of people is aggregated together and then has the opportunity to leave and go out if they choose to play in the retail market.

The second big issue for us we think is reducing pollution from our power plants and not choking our kids in the future. It is important to recognize that over two-thirds of the coal plants in this country are grandfathered and do not meet today's current standards. And if we were to require them to meet those standards, three-quarters of significant pollution that is choking our cities would be eliminated. We think that this is an opportunity to clean up the air over our cities.

We think that we need to ensure that new energy sources are developed for our future. And, as we mentioned, we appreciate the renewables portion of your bill, but we think the way to go about it is through a renewables portfolio standard and a small public benefit trust fund.

We think that we need to enhance competition, if possible, and help consumers save money through enacting strong energy efficiency provisions.

And, last, we need to prevent just uncuffing the monopolies and give consumers new tools and strong tools to assure that we are able to deal with market power.

Let me go to the first point.

We think that the problem with the aggregation provision that is in your bill today is that it puts all the transaction cost on those that are not going to be able to afford them—the associations or the local government agencies that may choose to try and put together a package of electricity to sell to consumers.

And what it does is it creates an impenetrable barrier of high marketing and transaction costs that will functionally prevent that kind of aggregation from benefiting any except the trade associations and perhaps a few rural communities.

Many States have taken a look at this issue and have said the cost of switching a customer is high, and so high that we think the way to go about it is what they have done in Ohio and Massachusetts—allow the community to have a great debate and say, "Do we want to serve the customers within our boundaries?" And if, after that debate, the answer is yes, then everybody in that community is part of that buying club and you have professional help in making a choice among the various offers made to that community for power.

And then, if somebody wants to go out and buy at retail, they have the opportunity to do so and can opt out and go play in the retail market.

Why is this important? After competition in Texas, 60 percent of us are still with AT&T. Most of us do not care enough about the nuances or the various differences in price to go out and shop. This is a real opportunity to lower the costs for everybody in that community.

The second thing we want to talk about, an incredibly important part of the issue for us is air pollution.

As I mentioned, two-thirds of our power plants are grandfathered. And, Mr. Barton, you asked a darned good question. Why is this not a State issue?

In Texas we said, "We are going to clean up our grandfathered power plants, require them to reduce emissions by 50 percent." And we decided that this—the reason we did this was because it was the most cost-effective way to reduce pollution in our State, far less expensive than even getting our cars inspected, and significantly less costly than buying reformulated gasoline or low-emission vehicles. It was a bargain that was worth doing.

But the problem is, what you heard time and time again from people in Texas is, "This is going to make us uncompetitive in the national market." That is why it is important that we set the standard across the United States to be the same.

If we were to adopt the current Federal new source performance standard, there would be dramatic reduction in pollution in the eastern United States. The "New York Times" reported on August 28 that if we adopted the Federal new source performance standard and cleaned up all those old power plants, industrial NO_X in

New York City would drop by 80 percent. That is the implication of this.

And if we do not do that, what we do is we drop our generating portfolio to the dirtiest common denominator, and we can do better than that.

Recently, a study came out—yesterday—called ''Out of Breath'' by a coalition called ''Clear the Air.'' This will be distributed to you all soon. It basically documents that 153,000 times a year somebody goes to the emergency room due to asthma. Power plants are the largest single cause of this.

And, last, I would make the argument that we need to do something better for renewable resources. The renewable portfolio standard would set a national goal that would enable us to have energy independence, be able to reduce the cost of these resources, be able to produce a product we can sell to the emerging countries who are not yet hooked up to the grid, and get us away from the single fuel dependence that we are rushing toward at headlong speed because everybody is buying and building natural gas plants.

I am old enough, as you are, Mr. Chairman, to have been in Texas in the days when we could not get natural gas for our power plants, and that caused us to make the mistakes that have caused us to have the stranded cost problem today, to build those nuclear plants, to build those coal plants, and to go down the wrong path. But the wrong path does not need to be replicated, and we are about to do that unless we require fuel diversity in our mix, and we believe that having a set-aside of 10 percent for renewable energy by 2010 is a good way to do that and a cost-effective way.

Thank you for your time, and thanks for the invitation.

Mr. BARTON. Thank you, Mr. Smith.

We now want to hear from Mr. Tom Casten, who is president and CEO of Trigen Energy Corporation headquartered in White Plains, New York, but I am told he is a constituent or at least a personal friend of Congresswoman Karen McCarthy of Missouri, who wanted to introduce you to the committee, but she is apparently still on the floor in the roll call vote. So when she comes back, if she comes back and this panel is still here, we will give her an opportunity to brag on you a little bit.

Your statement is in the record in its entirety, and we recognize you for 6 minutes to summarize it.

STATEMENT OF THOMAS R. CASTEN

Mr. CASTEN. Thank you, Mr. Chairman. I am going to leave my statement in the record and you can look at the things there.

I was struck this morning by your comment that it was easier on this side, and that you and the panel have to wrestle with competing ideas and philosophies and sort something out of all of this. I think I can provide one comment that might help you sort through those competing ideas, and then—you before have complimented people on providing facts as part of their answer, and I would like to present a couple facts.

One of the things that I have heard on this and earlier panels very consistently is that we have one point that we all agree about: we do not want competition in our part of the business. I completely agree with that. I find it is a horrible, evil force for any

businessman. I lay awake at night trying to think about how to innovate and how to cut my costs, and I cannot get that done. We have to give up profits. And I would be very pleased if this bill would simply say, ''Nobody can compete with Tom Casten.'' And I would thank you for that.

My suspicion is that that is——

Mr. BARTON. We do not have anybody from Nebraska on the subcommittee or that would probably be an amendment.

Mr. CASTEN. My suspicion is that the goal of this panel and, indeed, the Congress is not to prevent people from competing with Tom Casten, and I do not think it should be to prevent people from competing with the members of the Edison Electric Institute or the American Public Power Association or the TVA or the RUS, but that the real goal is for you to unleash competition and get at the innovation.

With that said, let me present a couple facts.

I am that competition. As we sit here, there are some 200 small generators that we have installed in the last 20 years running in about half the States in the country—those that do not have laws against it.

We have 32 power plants in 18 States that serve multiple users, and I would just like to go through the facts of what those competitive power plants do in hopes that that might give this committee some idea of why you are going through all this heavy lifting and how big the goal is at the end of the day.

In 1998, those 31 power plants put out 46 percent of the criteria pollution that EPA said would have come from producing the same heat and power in a conventional way.

They save more than 30 percent of the fossil fuel that would have been burned doing it in a conventional way.

They are technology and fuel independent. We burn coal, we burn gas, we burn oil, we burn biomass, we burn municipal waste. I do not think Congress needs to tell us what to burn. We will burn whatever is cheapest if you give us the chance to compete.

Now, the common thing that I see in the press and I hear people talking about is to portray this whole process as what benefits will go to the individual as a purchaser of electricity in their home, and I think that is important, and competition will help those people, but I think it is the wrong question.

I would like to review with you where the benefits go from our plants.

In Philadelphia, our 150 megawatt cogen plant provides the thermal energy to virtually every educational institution, every higher educational institution—people like University of Pennsylvania, Drexel, Thomas Jefferson—and that lowers the cost of tuition and education.

In Tulsa, Oklahoma, we provide that kind of savings to all of the city buildings.

In Kansas City, we provide it to city, State, county, and Federal buildings. Kansas City even uses us as a way to meet their air quality rules, because we are so much less polluting that they do not have to force carpooling. So the benefits go to lowering the taxes that people pay for government.

We serve some 26 hospitals, and we save them between 20 and 40 percent of what they would have paid, and this lowers the cost of medical care to everybody.

If those benefits are not persuasive, I can tell you that we do some really important things. In Golden, Colorado, we cut down the cost of making a can of beer.

Those benefits go to everybody.

What I believe is in front of this panel is to understand what can happen if you continue with your good work and get a bill passed.

Our estimates are that the U.S. consumer will save more than $100 billion a year with competition. Our estimates are that the air quality will come into compliance everywhere just through competition.

We believe that the competitiveness of every U.S. manufacturer will improve by reducing the cost that they pay for energy.

I just leave you with a thought. Where would we be today without competition in other places? Maybe only 60 percent of the people still stay with AT&T, but I suspect 60 percent of the people in this room have a cell phone because Craig McCall could compete and was not forced not to.

Where would we be in computers if Michael Dell was not allowed to compete and say, "I have got a different way to do it"?

The challenge that I think this panel has is to get a bill out that will let everybody compete, and then just stand back and enjoy, because it will be fun to watch.

Thank you.

[The prepared statement of Thomas R. Casten follows:]

PREPARED STATEMENT OF THOMAS R. CASTEN, PRESIDENT AND CEO, TRIGEN ENERGY CORPORATION

Mr. Chairman and members of the Subcommittee, thank you for allowing me to testify before you today on H.R. 2944, the Electricity Competition and Reliability Act of 1999.

My name is Tom Casten, and I am the CEO of Trigen Energy Corporation. Trigen specializes in generating energy very efficiently. We own and operate the most efficient power plants in the world, and our stock in trade is combined heat and power, or CHP.

We have thirty-three projects, with operations in nineteen states, Canada and Mexico. We joint venture with many companies, including electric utilities such as Cinergy and Pepco. Since I last testified before this subcommittee, Trigen has announced several major new projects and has won two very satisfying industry awards, including an award from the National Council for Public-Private Partnerships and the Power Plant of the Year Award from McGraw-Hill.

Mr. Chairman, our projects and our people are at work every day showing how efficient energy production is both good for business and good for the environment. By restructuring the electricity industry, Congress can reward investors, benefit consumers, strengthen our economy and clean up our air, land, and water. As you know, I've had the privilege of appearing before this Subcommittee and other House committees to share my thoughts on the important economic and environmental benefits of electricity restructuring. Rather than restate those comments, I have attached copies of my previous testimony to these remarks and ask that they be made part of the record of this hearing.

Chairman Barton and the Members of the Subcommittee, thank you for pushing forward on electricity restructuring. This is an issue of critical importance to our industries, to the wholesale and retail consumers of electricity, and to the global competitiveness of the United States. Competition is already upon us, with the States leading the way. The Federal government must rise to the task of completing this nationwide effort by addressing those barriers to competition that inherently lend themselves to national legislation, matters that cannot be responsibly dealt with in a piecemeal, State-by-State way.

It is evident that H.R. 2944 is the result of painstaking, thoughtful work that reflects the benefit of numerous hearings, consultations, examination of issues by the Subcommittee's working group, and input by incumbents and independents, the States, the Administration, consumer groups and others. H.R. 2944 marks a critical step in efforts to improve electricity markets and we offer our support for its enactment.

As I read the bill, it strikes me, however, that the current language should be modified with regard to the following five issues: interconnection, PURPA repeal, CTC's , depreciation schedules, and tax incentives. I'll discuss the changes we think you should make, and have attached to my testimony specific amendatory language for your consideration.

Interconnection

H.R. 2944 correctly recognizes the economic and environmental importance of new distributed generation, including CHP systems, by addressing the central issue of interconnection. Current charges for interconnection can be prohibitively and unreasonably expensive, and requirements vary arbitrarily from State to State, utility to utility, site to site. Incumbents who do not want to face competition often attempt to cloak anticompetitive behavior in the guise of technical disagreement over interconnection. It's essential for interconnections to be safe and reliable, but let's take the market gamesmanship out of electrical engineering. Bringing uniformity to interconnection through national technical standards will reduce uncertainty, lower costs, and facilitate deployment of modern generation, including CHP technology, across the country.

Interconnection language must be sufficiently broad to help all appropriately sized generators connect to the distribution grid. I am concerned, however, that the present language of§ 542 may be too limiting, and will retard the ability of the nation to realize the substantial economic and environmental benefits offered by CHP and other new generators. For example, the present language apparently does not apply to third-party owned systems, systems currently designed to serve wholesale customers, or systems designed for off-site sales of electricity. It should give you some sense of the unduly narrow scope of the current language to note that it would appear to benefit few of my company's projects.

Let me give you an example of the interconnection problem. We know how to interconnect generators with the distribution grid. We have done it literally dozens of times. Technically, it is a pretty straightforward task. In 1997, my company approached a Maryland utility to request interconnection for a 703 kw generator to be installed in a downtown Baltimore office building. The small system would supply the building's electric load and air conditioning. Yet, two years later, we were still dickering with the utility over so-called "technical" issues. Months after receiving our initial request for interconnection, the utility asked that Trigen design a different, specialized interconnection. Trigen completed the new design at an additional cost of $44,000. The utility rejected the design. In response, Trigen offered to use guidelines developed by Consolidated Edison in New York City, even though the ConEd guidelines were disproportionately burdensome and expensive given the very small size of the installation. The utility agreed, but after Trigen complied with these requirements, the utility imposed further "technical" restrictions on Trigen's ability to operate the facility. These disagreements have only recently been resolved, at a great cost to Trigen and our customer. One would strongly suspect that this was anti-competitive behavior masquerading as technical disagreement which successfully prevented the unit from operating for two years. H.R. 2944 would not fix this sort of problem, and thus needs to be amended.

Prospective Repeal of PURPA's "Must-Sell" Provision

H.R. 2944 would repeal both the "must buy" and the "must sell" requirements of Section 210 of PURPA. Trigen does not challenge elimination of the "must buy" provision, but the "must sell" provision absolutely should not be repealed until all retail markets are competitive and until back-up power can be purchased competitively. That's not the case now, and until those fundamental changes are made, the utility should continue to be required to provide back-up power for qualifying facilities. The current language of § 531 would harm competition. Elimination of PURPA's "must sell" requirement before laws are changed to allow new facilities to purchase back-up power competitively will leave new entrants at the mercy of the local utility, subject to discriminatory pricing or outright denial of back-up power. Let's not take a step backward.

Elimination of Competitive Transition Charges

Trigen recognizes that utilities should be able to recover prudently incurred, legitimate and verifiable stranded costs that cannot be reasonably mitigated. How-

ever, States should be required to consider reducing the stranded cost charge on an electric consumer which efficiently produces energy on-site by a fuel cell or a combined heat and power, distributed power or renewable power facility. Such a provision would be consistent with an overall agenda of promoting clean and efficient power generation without imposing a mandate on States. Trigen believes that the relevant language contained in section 101 of the restructuring proposal submitted by the Administration would be an appropriate amendment to this legislation.

Tax depreciation schedules

The tax code currently does not allow depreciation of CHP and distributed generation technologies in a way that matches how the technology is actually used. This inappropriate treatment discourages investments in these technologies. For example, the IRS allows a gas turbine located inside a building for on-site generation use to be depreciated over a 39-year period. The same piece of equipment used for transportation (e.g., on an airplane) depreciates in one quarter of the time. The moving parts of the turbine used for electricity and heating may be replaced as many as three times while the owner continues to depreciate the original investment. Shortening the time over which this equipment depreciates would remove an impediment to investment in what is otherwise an efficient and environmentally beneficial technology.

The Administration's restructuring proposal included a provision that would shorten the depreciation period to 15 years. While we were grateful for the Administration's recognition that new distributed generation and CHP systems should not be subject to a depreciation period of 39 years, the approach failed to recognize that a one-size-fits-all class life for energy equipment is a fundamentally flawed approach which will grow increasingly anachronistic by the month.

New and small turbines have different physical properties and will generally operate under quite different conditions than large turbine units employed by traditional electric utilities and, consequently, will have different service lives. Further, the competitive marketplace will force energy suppliers to replace or "upgrade" standing equipment before it fails, since installation of more efficient technology offers lower costs to customers and the opportunity to hold or capture market share for competitive energy suppliers. We expect that energy generation equipment will come and go in the marketplace in a manner that strongly resembles that of modern computers " assets which outlive their economic lives long before they cease to work properly. Because these new and efficient technologies have different "actual" lives, they should not be subject to a single class life in the code. Accordingly, we have attached to this testimony modifications to the Internal Revue Code which would add new schedules of class lives for key energy generation technologies.

Combined Heat and Power Investment Tax Credit

Tax credits are typically offered by the Federal government to obtain public benefits by prompting private parties to make economic choices that they would not so readily make otherwise. As such, an investment tax credit is a good short-term mechanism to promote CHP systems, which offer very significant public and private economic and environmental benefits, but can often be more difficult for the private sector to deploy than electric-only projects because of the complexity inherent in assembling a "thermal load" or set of heating/cooling customers. We believe it is appropriate to enact a short term tax credit to assist deployment of new, modern generation while longer term solutions to competitive barriers are being developed, such as adjustments to the depreciation schedule, as discussed above. To be clear, to the extent the depreciation treatment of CHP is corrected, we do not believe that a tax credit will be necessary. However, to the extent a lesser fix is chosen for the depreciation treatment of CHP, the tax credit would remain an important short-term incentive for CHP system deployment.

Conclusion

Given the inevitability of competition in the electricity market, and both national and global trends that will guide the future of energy production in this country, I believe that emerging technologies are serving and will serve an indispensable purpose in meeting goals of energy efficiency and environmental demands. I urge this subcommittee to pass a strong, balanced restructuring bill reflecting the concerns I have raised here today. I thank the subcommittee for the opportunity to appear before you. Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Mr. Casten. We appreciate your work that you have done in your company providing services for the communities that you are in and appreciate your testimony.

Now we would like to hear from our last witness, Mr. Scott Segal. Apparently, he is just representing Bracewell and Patterson.

STATEMENT OF SCOTT H. SEGAL

Mr. SEGAL. Yes, we are a potent player in the electricity area.

Mr. BARTON. The only law firm that has its own lobbyist just on this issue. That is pretty interesting.

Mr. SEGAL. The new alternative energy source.

Mr. BARTON. Actually, I am told you are representing contractors. Your statement is in the record in its entirety. We recognize you for 6 minutes.

Mr. SEGAL. Thank you, sir.

Good afternoon, Chairman Barton and members of the subcommittee. My name is Scott Segal, and I am an attorney with the law firm of Bracewell and Patterson here in Washington and a proud native of the great State of Texas, I might add.

I also serve as outside counsel for the Air Conditioning Contractors of America, and we are appearing today on behalf of the National Alliance for Fair Competition, of which ACCA is a member.

The alliance is composed of 10 trade associations, and was formed especially to draw attention to the problems of small service contracting businesses with respect to unfair competition from public utilities and their unregulated affiliates. Many of our members are family owned and operated companies.

As the subcommittee has considered electricity restructuring legislation, I know that each of you has been barraged with information on a bewildering array of topics, such as stranded cost, transmission access, and the like. The Alliance is concerned that in this thicket of complexities the issue of cross-subsidization and other forms of anti-competitive conduct and their impact on small businesses has been lost.

My job today is to attempt to clear away the underbrush and present you with a simple message: Congress must address cross-subsidization and related unfair monopoly practices if you are to create a framework in which competition can flourish, and you can do so without giving undue power to Federal regulators or interfering with State prerogatives in this area.

Mr. Chairman, what is this whole debate about electricity restructuring all about? Well, in my view it is about creating the conditions for competition in the electric power industry so that the American consumer will benefit from more choice, better service, and lower prices. The members of our alliance strongly support full competition. We are fully accustomed to competition, do not seek subsidies or special treatment in order to compete. Similarly, we do not believe that utility affiliates competing in service industries should enjoy cross-subsidies derived from their parent companies' monopoly power. To allow these practices to go unchecked will destroy, or at least potentially harm, the goals of full competition, and, subsequently, shortchange consumers.

We do not oppose utility diversification. In fact, we welcome the competition. However, ensuring vigorous competition and benefits to consumers will take place only if the legal framework ensures the competition is open rather than dominated by the vestiges of this monopoly status.

I would illustrate my point—and with all due respect to Mr. Casten—ours are member companies that do not fear competition. We think we are competition.

I brought along with me a local telephone directory, which I would now like to read into the record. No, just kidding. This is a local telephone directory from northern Virginia. If you look up air conditioning contractors in here, there are 31 pages of listings. If you look up electric utility, there is one—not page, one listing.

The point I am trying to make is: do we want the market for energy services to look more like the former or the latter? We know competition and are not afraid of it.

Mr. Chairman, I know that as you have proceeded you have been rigorous limiting the content of the bill to matters in which Federal action is necessary. I submit to you that establishing some standards in the area of affiliate transaction meets this litmus test.

First, antitrust law, a traditional area of Federal responsibility, does not address cross-subsidization and related practices adequately. There is a long-established role for the Federal Government in antitrust policy; however, both the Department of Justice and the Federal Trade Commission have testified that antitrust laws are ill-suited to addressing existing market power resulting from the previous regulated monopoly status of electric utilities; therefore, existing antitrust law is not sufficient. Indeed, this Congress recognized the need to enact stringent affiliate safeguards in the Telecommunications Act of 1996.

Our alliance seeks only to assure that minimal protections against market power abuse are enacted and that States remain free to achieve these ends in the manner they see fit.

Second, unregulated competitive affiliates will operate across State lines. Suffice to say that electric utilities exist across State lines and they offer affiliate services across State lines, so a national solution is justified.

Further, the availability and application of State remedies to claims of competitive harm is uneven, at best, and even within States there is typically a division of authority between State PUCs, which are charged with protecting ratepayers, and antitrust enforcement agencies, which are charged with enforcing restriction on anticompetitive practices.

We go to either one, and both say we are going to the wrong agency, and that can get frustrating for a small business.

Ultimately and fortunately, we believe that Federal guidance on cross-subsidization and self-dealing will complement rather than supersede State action. The alliance is simply seeking to ensure that competitive issues confronting small business and the people they serve do not fall between the cracks.

I want to make crystal clear, we are not asking the subcommittee to dictate the details of State codes of condition; rather, we seek broad policy principles that are essential to guaranteeing competition while continuing to allow the States the utmost freedom to innovate.

Accordingly, our members believe that the legislation can be improved by the addition of a few minimum standards.

First, a clear prohibition on cross-subsidization of competitive affiliates.

Second, a requirement that States develop codes of conduct and that they be applied to all affiliates, but note I say that States develop it.

Next, a requirement that competitors harmed by cross-subsidies and anticompetitive conduct have recourse to State PUCs.

And, last, a requirement that enforcement include a remedy for harm to competitors occasioned by such unfair competitive practices.

Again, I must emphasize our alliance is not advocating that Congress prescribe the details of codes of conduct for utility affiliates, nor are we asking that Congress provide broad new powers to Federal agencies like the FERC or anybody else. Rather, we are asking that Congress set broad policy goals which represent a minimum, a floor, to ensure free and open competition.

Well, as they say in the refrigeration business, we just hope you do not freeze us out of the bill.

I thank the members of the subcommittee for this opportunity to appear before you today, and we look forward to answering any questions you may have.

[The prepared statement of Scott H. Segal follows:]

PREPARED STATEMENT OF SCOTT H. SEGAL ON BEHALF OF THE AIR CONDITIONING CONTRACTORS OF AMERICA AND THE NATIONAL ALLIANCE FOR FAIR COMPETITION

Good morning Chairman Barton, Congressman Hall and members of the Subcommittee on Energy & Power. My name is Scott Segal and I am an attorney with the law firm of Bracewell & Patterson here in Washington, D.C., and serve as outside counsel for the Air Conditioning Contractors of America (ACCA). I'm also appearing today on behalf of the National Alliance for Fair Competition (NAFC), of which ACCA is a member. The National Alliance for Fair Competition is composed of ten national trade associations. NAFC was formed specifically to draw attention to the problems small businesses face with respect to unfair competition from public utilities and their unregulated affiliates.

The organizations which comprise NAFC consist, overwhelmingly, of small, private sector businesses engaged in the design, supply, sale, rental, installation and servicing of electrical and mechanical products, equipment, and systems, as well as providing energy fuels. These firms operate in residential, commercial and industrial markets. While a few larger firms are included within the group, the majority of businesses are small. Many are family owned and operated.

As the Subcommittee has considered electricity restructuring legislation, I know that each of you has been barraged with information on a bewildering array of topics such as stranded costs, transmission access, the role of the federal power administrations, and others. Each issue has its own complexities. NAFC is concerned that in this thicket of complexities, the issue of cross-subsidization and other forms of anticompetitive conduct and their impact on small business has been lost. My job today is to clear away the underbrush and present you with a simple message: Congress must address cross-subsidization and related unfair monopoly practices if you are to create a framework in which competition can flourish, and you can do so without giving undue power to FERC or interfering with state prerogatives in this area.

During the course of the Subcommittee's hearings on this issue, you have been presented with testimony from contractors and other working people regarding the types of practices that allow incumbent utilities to unfairly leverage their market power in competitive markets, such as heating, ventilating, air conditioning and refrigeration (HVACR) services. I do not intend to revisit these issues in detail, but provide a representative list of the types of conduct that concern small business including cross-subsidies to and preferential treatment of affiliates. This encompasses: shared customer data, equipment, vehicles and personnel, cost-shifting, marketing data, free advertising for affiliates, preferential referrals, discriminatory access and pricing of services, and similar uncompensated transfers of tangible and intangible benefits.

I will focus my testimony on the following points: (1) cross-subsidization and other anticompetitive practices harm consumers and competition; (2) there is a need for

federal legislation to create a framework for competition and precedent for doing so; (3) Congress can set minimum standards to achieve the goals of competition without stifling state innovation; and (4) H.R. 2944 does not currently go far enough to address these issues.

Getting Back to Basics: Creating the Conditions for Competition

I would like to return to first principles for a moment. What is the debate over electricity restructuring all about? It's about creating the conditions for competition in the electric power industry so that the American consumer will benefit from more choice, better service and lower prices. The members of the NAFC strongly support full competition. We are fully accustomed to competition and do not seek subsidies or special treatment in order to compete. Similarly, we do not believe that utility affiliates competing in service industries should enjoy cross-subsidies or other advantages derived from their parent company's monopoly power. To allow these practices to go unchecked will destroy your goals of full competition and subsequently, short change consumers.

As a deregulated retail market for electricity takes shape, incumbent utilities feeling competitive pressure are increasingly driven to diversify into energy services and other affiliate activities. For instance, if you go to the Pepco webpage, you will find a link to Pepco Energy Services. This webpage states, "Pepco Energy Services is backed by the strength, stability and commitment of its parent company, which has a 100-year history of delivering quality customer service."[1] The same webpage describes Pepco Energy Services' ability to design and install HVACR systems, lighting and other energy equipment, and a full range of services performed by contractors today. NAFC does not oppose this diversification, and in fact, welcomes the competition. We are, however, concerned that as many regulators have recognized, "there is a strong incentive for regulated utilities or their holding companies to subsidize their competitive activity with revenues or intangible benefits derived from their monopoly businesses . . ."[2]

In creating a framework for competition, the Subcommittee must be mindful of the background against which you are legislating. Competition is not starting from the level playing field characteristic of a newly developing market, but rather, with regulated monopolies. Ensuring vigorous competition and benefits to consumers will take place only if the legal framework ensures that competition is open rather than dominated by the vestiges of this monopoly status.

As I mentioned, the NAFC believes that cross-subsidization and other anti-competitive practices are bad for consumers and bad for competition. Here's why:

- *Bad for Consumers:* Cross-subsidization and preferential self-dealing will artificially increase the costs of the regulated utility as costs incurred for the benefit of the affiliate are shifted to the regulated firm. These higher costs will be passed on to consumers in increased prices in the regulated market. In addition, these practices will increase costs in unregulated markets like those for HVACR services by displacing innovative, lower-cost suppliers and entrants with a higher-cost affiliate of the incumbent utility which can undercut pricing due to the subsidy that it enjoys.
- *Bad for Competition:* Competition thrives in an environment where numerous entrants compete on choice, price and quality of service for consumers. Yet, as we make the transition to a competitive environment, there are strong incentives for regulated utilities or their holding companies to subsidize their competitive affiliates with revenues or intangible benefits derived from monopoly businesses. These benefits allow the affiliates to drive lower-cost providers from the market and to deter new entrants into the market. This results in less competition and less choice for consumers.

To illustrate my point, I have brought along with me today a local telephone directory. In this Northern Virginia directory, I find thirty-one pages of entries for HVACR contractors. By contrast, I find only one entry under "electric company." Do we want the market for energy services to look more like the former or the latter?

Why is Federal Legislation Necessary?

Mr. Chairman, I know that as you have proceeded to develop consensus legislation you have been rigorous in attempting to limit the content of the legislation to matters in which federal action is necessary. I submit to you that establishing some standards in the area of affiliate transactions meets this litmus test.

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[1] See <http://www.pepco-services.com/>.

[2] Promulgation of New Rules Governing Activities Between Affiliates, Public Utility Commission of Texas, Project No. 17459, 23 Tex. Reg. 5294 (May 22, 1998).

- *Antitrust law, a traditional area of federal responsibility, does not address cross-subsidization and related practices.* While the federal government shares authority over enforcement of the antitrust laws with the states, there is a long-established federal role due to the impact of competition policy on interstate commerce. Yet in testimony before this Subcommittee, representatives of the Antitrust Division at the Department of Justice and the Federal Trade Commission, the principal agencies charged with enforcing the antitrust laws, have testified that the antitrust laws are ill-suited to addressing existing market power resulting from the previous regulated monopoly status of electric utilities.[3] Therefore, leaving the competitive implications of market power abuses affecting small business to the antitrust laws is not sufficient. Indeed, this Congress recognized the need to enact stringent affiliate safeguards in the Telecommunications Act of 1996 to prevent the opportunity for market power abuses by the Bell operating companies to the benefit of their affiliated competitive businesses. Some of these provisions included requiring separate affiliates, biennial audits, restrictions on joint marketing, prohibitions on preferential treatment to name just a few. By contrast, NAFC seeks only to assure that certain minimal protections against market power abuse are enacted and that states remain free to achieve these ends in the manner that they see fit.
- *Unregulated, competitive affiliates will operate across state lines.* The presence of these unregulated affiliates in several states will present new difficulties for individual state commissions, and it is unlikely that the limited jurisdiction of state bodies will be well-suited to ensure fair and open competition when multistate holding companies are involved. State commissions frequently lack the authority and resources to pursue these issues effectively. It is unrealistic to expect a nationwide energy market to develop without national legislation to ensure true, fair retail competition.
- *The availability and application of state remedies to claims of competitive harm is uneven at best.* Because the electric power industry has been regulated for most of this century as a local monopoly, state regulators have been concerned primarily with issues related to ratepayer protection and ensuring an appropriate rate-of-return. In the newly emerging competitive environment, there will be an increasing need to pay close attention to issues of competition and competitive harm occasioned by unfair practices such as cross-subsidization.
- *There is a division of authority between state PUC's, charged with protecting ratepayers, and antitrust enforcement agencies charged with enforcing restrictions on anticompetitive practices.* Indeed, in some states, affiliate codes of conduct have been held not to apply to all competitive affiliates, but only to marketing affiliates.
- *Small business is often left without an effective remedy for competitive harm.* As a result, small businesses harmed by anticompetitive practices are often left without a remedy. While state PUC's have the ability to deny a rate increase or, in an extreme case, impose a fine, these remedies have little meaning for competitors harmed by cross-subsidization and related practices. As previously noted, the antitrust laws are similarly ill-equipped to address concerns arising from existing market power. Therefore, those harmed by anticompetitive practices are left without a remedy.
- *Federal guidance on cross-subsidization and self-dealing will complement rather than supersede state action.* In moving from an electric power industry characterized by local monopolies to one in which there is unfettered competition, the NAFC is simply seeking to ensure that competitive issues confronting small businesses and the people they serve do not fall between the cracks. I wish to make crystal clear that we are not asking this Subcommittee to dictate the details of state codes of conduct. Rather we seek to see enacted certain broad policy principles that are in our view essential to guaranteeing the creation of a free and open competition while continuing to allow the states the utmost freedom to innovate to achieve these policy objectives.

H.R. 2944 and the Need to Address Affiliate Safeguards

To the extent that H.R. 2944 addresses affiliate transactions, please refer to Title V of the bill, and in particular in sections 513, 514 and 516. Sections 513 and 514 of the bill take the important first step of ensuring that federal and state regulators

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[3] *Electricity Competition: Market Power, Mergers and PUHCA*, before the Subcommittee on Energy & Power of the Committee on Commerce, U.S. House of Representatives, 106th Cong. (May 6, 1999) (statement of Mr. Douglas A. Melamed, Antitrust Division, United States Department of Justice, and statement of The Honorable Mozelle Thompson, Commissioner, Federal Trade Commission).

have access to the books and records of utilities and related companies for the purpose of assessing costs incurred to protect ratepayers. Section 516 of the bill entitled "Affiliate Transactions" serves merely as a savings clause which states that nothing in the legislation shall preclude the application of other existing law to determine whether costs of an activity performed by a related company may be recovered in rates. In other words, this provision preserves the status quo.

Yet, as I have detailed above, the status quo is not sufficient to promote truly open competition in energy services markets, and this will ultimately be to the detriment of the American consumer. The lack of federal or state protections that provide an adequate remedy in these areas and the increasingly interstate nature of these operations demands congressional attention. Accordingly, the members of the NAFC believe that federal legislation should at a minimum take the following modest steps, including:

- a clear prohibition on cross-subsidization of competitive affiliates;
- a requirement that states develop codes of conduct and that they be applied to all affiliates equally;
- a requirement that competitors harmed by cross-subsidization and other anti-competitive conduct have recourse to the state PUC for a remedy; and
- a requirement that enforcement include a remedy for harm to competitors occasioned by such unfair competitive practices.

Again, I must emphasize that the NAFC is not advocating that the Congress prescribes the details of state codes of conduct for utility affiliates. Nor are we asking that Congress provide broad new powers to federal agencies such as the FERC. Rather we are asking that Congress set certain broad policy goals to ensure free and open competition in the market for energy services which are inextricably bound up with this debate. These broad policy goals represent basic tenets of a competitive marketplace which Congress has seen fit to protect before to ensure that the benefits of competition are available across the country. The states have, and should continue to, be free to devise innovative solutions to achieve these basic objectives of competition.

I thank the Members of the Subcommittee for the opportunity to appear before you today. I hope that many of you will agree that some congressional action in this area is appropriate, and look forward to answering any questions that you may have.

Mr. BARTON. We do appreciate that. You may get a chilly reception on your use of metaphors, but we are going to work on it. Thank you, Mr. Segal, for that testimony.

The Chair is going to recognize himself for 5 minutes for questions.

Mr. Brice, you used a term that I am not familiar with in your testimony. You talked about you wanted a "truth in billing" requirement. Could you, in layman's terms, express to me what "truth in billing requirement" means in terms of this bill?

Mr. BRICE. I think what we are—I am at a loss, myself, to really explain what that means.

Mr. BARTON. Well then just give it to us for the record, because Congressman Hall did not know, I did not know, my staff did not know. Whoever wrote your testimony hopefully does know.

Mr. BRICE. Yes, I am sure they do.

Mr. BARTON. And we are open to it, if we understand what it is, because who can be against truth in billing? I mean, it kind of, on its surface, appears to be a good idea. So if you will just get that to us for the record.

Mr. BRICE. Yes, Mr. Chairman.

Mr. BARTON. Okay.

Ms. Moler, I am going to ask you a cheap shot question, but I am going to tell you up front that it is a cheap shot question, because I do not mean it personally, but I was struck by some of the terminology in your testimony. You talked about the crazy quilt of regulation.

Who was the chair of FERC in 1996?

Ms. MOLER. I was.

Mr. BARTON. You were.

Ms. MOLER. Yes, sir.

Mr. BARTON. Okay. I thought so. When was FERC Order 888 issued?

Ms. MOLER. In 1996, when I was the chairperson.

Mr. BARTON. In 1996, when you were Chair. Now, remember, I told you up front this is a cheap shot question.

Ms. MOLER. I will not give you a cheap shot answer. I will give you a serious answer.

Mr. BARTON. I know. Do not we codify, if the bill before us were to become law, do not we codify the crazy quilt regulatory scheme that FERC Order 888 put in place in 1996 when you were chair of the FERC?

Ms. MOLER. Mr. Chairman, as my statement acknowledges, Order 888 applies to wholesale transactions and to unbundled retail transactions. It does not apply to bundled retail transactions.

Mr. BARTON. I mean, that is what——

Ms. MOLER. At the time we issued the order, there was one State that had customer choice enacted. The world has changed very, very significantly since Order 888 was enacted. So I am and Americans for Affordable Electricity believe that at this point, with the industry having evolved the way it has evolved, that you need to go farther than Order 888.

Mr. BARTON. But you admit——

Ms. MOLER. I recognize that it does codify Order 888. I recognize that, sir, but I also——

Mr. BARTON. So I am in agreement with where you were in 1996. I am just not in agreement——

Ms. MOLER. Well, I am hoping you will come along.

Mr. BARTON. [continuing] yeah with where you are in 1999.

Ms. MOLER. I am hoping you will come along. The crazy quilt that has evolved has very little happening under the Order 888 tariffs, and we simply need to go farther at this point to encourage further competition. But it does codify it. Yes.

Mr. BARTON. Okay. Well, I do not mean that personally, you know. I want you to know that. I would not—that just kind of struck me the way you put it that I needed to chastise you a little bit, but I understand——

Ms. MOLER. Well, one of the challenges in these jobs is you have to look at changed circumstances——

Mr. BARTON. That is true.

Ms. MOLER. [continuing] to figure out what the appropriate response is under the changed circumstances.

Mr. BARTON. Now let me ask you another question. And this is not a cheap shot question. Why will not the bill, as it is drafted—we have mandatory participation in RTOs. They have to join RTO's. We give the States regulation of bundled rates, and the States I think—I think the States will do a better job of looking at that issue than the group that you represent do—and we still have the Federal antitrust regulatory scheme that is in generic law. So why won't that combination of mandatory RTO participation, State regulation of bundled sales at retail, and Federal anti-

trust law that is still on the books, why doesn't that solve the market power problem if there is a market power problem?

Ms. MOLER. Until you require everyone to be under the same rules for transmission, you are not going to get the much-revered level playing field.

Mr. BARTON. But the RTO is regional.

Ms. MOLER. The RTO would not require all of the utilities' use of its system to be subject to its requirements.

Mr. BARTON. But it does require every utility who participates in that RTO to be subject to the rules for that RTO.

Ms. MOLER. Sir, there are many RTOs—ISOs now—for which the vast majority of the utilities' use of its transmission system are not under their jurisdiction.

Mr. BARTON. Okay. Well, I——

Ms. MOLER. I was stunned, frankly, when I learned this. I, too, thought we had done a great thing with Order 888, and I still believe it was a great thing.

Mr. BARTON. Well, you did a good thing.

Ms. MOLER. But what we are learning in the actual——

Mr. BARTON. We are doing a great thing in our bill. You did a good thing in Order 888.

Ms. MOLER. Well, I encourage you to even greater greatness.

Mr. BARTON. Okay.

Ms. MOLER. What we have learned is that until you put all of the uses of the same kinds of facilities under the same rules, that you are not going to get comparability and you are not going to get the kind of competition that will serve the public.

Mr. BARTON. Okay. I want to ask Mr. Smith a question because my time has expired, and then I am going to go to Ms. McCarthy, if she wants to introduce Mr. Casten after the fact.

Mr. Smith, you talked about an opt-out preference for aggregation, which sounds to me suspiciously like forced municipal aggregation. Why are you not satisfied with our opt-in aggregation provision which gives people the voluntary right—and not just city governments, but any group to aggregate in a State that is open?

Mr. SMITH. I was hoping you would ask me that question.

Mr. BARTON. I bet you were. That is why I asked it.

Mr. SMITH. And the other argument, of course, that I expected was, "Well, is not this just State-sanctioned slamming." I think there are two answers to that. One is, we are not going to make anybody change unless the community has a great and robust debate over whether or not they ought to serve as that aggregator.

And the genius of democracy is at the smallest levels, where people can have that debate as to whether or not they do want to create a new municipal utility or whether their county government should serve them, or out in the rural areas of Texas, beyond where you and I both live, whether or not the school district or the councils of government perhaps could serve them at lower cost.

And I think that is the—in our question, in our minds, as we have begun to look at this as to whether or not we are better off in those instances having new municipals created, or what opportunities this gives us, that debate is what gives us comfort that it is not just forced municipalization.

The other key component to this, sir, is——

Mr. BARTON. You could have a 51/49 debate, though, or a 52/48.

Mr. SMITH. You sure could.

Mr. BARTON. I mean, there is—democracy is a wonderful thing, but I see votes on the floor almost every week that are 218 to 217, or very close to that.

Mr. SMITH. And I am usually on the losing side of it, but I understand that democracy——

Mr. BARTON. Well, we want to keep it that way.

Not really. I retract that.

Mr. SMITH. And, Mr. Barton, the other thing that scares me to death is putting this to a vote when you have got the big utilities having the right to fund the elections against you. I understand that this is a big issue, and it is a gut call for all of us that we think is worth doing.

But I think that is the point. We think it is worth doing, and, as people have looked at how to make this work best for consumers, there are those situations where new creations of government make the best sense. That was what happened two generations ago when our grandfathers electrified most of Texas or, in my case, Illinois.

They looked at the fact the most cost-effective way to do this was with a public aggregator.

Mr. BARTON. Well, we are for aggregation. Our bill has got, I think, a very strong and defensible aggregation provision in it. I am just not sure we want to go to the opt-out version that your group supports.

Mr. SMITH. And the reasons that we think that it is superior are two. One is it eliminates that solicitation and transaction cost that is essentially a barrier that prohibits many municipalities from going out and trying to aggregate and then switch consumers, because that has been an incredibly difficult thing, as we have seen, in just about every State that has gone to competition, to get people to move.

And, second——

Mr. BARTON. Be concise, because my time expired about 5 minutes ago.

Mr. SMITH. And that is probably the most concise thing is the cost barrier is so high that, unless you do it the other way—and the other point that I wanted to make is we do give people who want to go out and play in the retail market, who think there is a better deal out there for them, the opportunity to leave and go out and buy in the retail market, to join associations like mine or AARP or the big business association and go out and buy in those groups if they want to, or buy in the retail market, and so it is the best of both worlds, we think.

Mr. BARTON. Okay. The gentleman from—well, first the gentlelady from Missouri. Does she wish to formally introduce Mr. Casten to the committee?

Ms. MCCARTHY. Mr. Chairman, I am going to brag about him when it is my turn to ask questions.

Mr. BARTON. Okay. Then we are going to recognize the gentleman from Ohio, Mr. Sawyer, for 5 minutes for questions.

Mr. SAWYER. Thank you, Mr. Chairman.

Let me go back to Commissioner Moler and go back to the dead horse I keep beating in terms of transmission.

I hope it is not a dead horse, Mr. Chairman.

It seems to me that one of the things we keep hearing in one form or another is that people are deeply concerned about equality of access, and to make sure that transmission is not used as a conscious tool in advantaging one supplier over another, and in the end wind up cutting off markets.

It seems to me that you are probably a veteran of the California transmission wars. In fact, it was the head of the California Commission who at one point said that 100 years of transmission wars made the ISO a psychological necessity. That was before RTOs.

Putting those wars behind us, could you look into the future and speculate on what the success of stand-alone transmission entities might look like, the kind of things that the Transmission Alliance is talking about five, 10 years into the future?

Ms. MOLER. I believe that there are substantial pressures on utilities to look at what their core businesses are going to be. There is some interest in the industry in developing stand-alone transmission companies.

One of the challenges that we have in the industry today, as I look at it, and as my clients look at it, is that not all uses of that system are on the same tariff, and so there are dramatic differences in access, terms, and conditions, rates, preferences, all those kinds of things in terms of use of the same kinds of facilities.

Mr. SAWYER. Are you describing, in effect, the arenas of regulatory reform that would be required to enable the success of these kinds of structures?

Ms. MOLER. I believe that, in order to have a fully competitive market, transmission will continue to be a monopoly for the foreseeable future. I do not think we want two sets of wires down the interstate highways.

Distribution I believe will continue to be regulated by the States for the foreseeable future. And what we are seeing now is a diminution in wholesale transactions. We are seeing the wholesale market is not functioning well at all. We are seeing less trading now on NYNEX, for example, than you saw just a year ago. Things are headed in the wrong direction.

An economist I talked to yesterday said that he believes that on most systems that less than 10 percent of the use of the transmission lines is subject to Order 888 requirements. I was stunned by that number.

We have got to have more happening—same kinds of facilities, under the same set of rules.

Mr. SAWYER. Do we need to encourage investment?

Ms. MOLER. Absolutely.

Mr. SAWYER. Can you talk about the kind of encouragement that we ought to provide?

Ms. MOLER. Americans for Affordable Electricity does not have a particular position on incentive rates versus traditional rate-making approaches. I think there is some experimentation going along.

I can tell you from experience that it is difficult to develop an incentive rate structure that really works.

Mr. SAWYER. In one point in your testimony you analogize to—is it Order 668?

Ms. MOLER. Order 636 is the gas equivalent.

Mr. SAWYER. That is what I meant, the natural gas order. Does that analogy extend to citing decisions, as well? Should it? And, if not, what is the solution to the conundrum that we face with regard to——

Ms. MOLER. AAE does not have a position on this. I, personally, have testified before this committee that I believe there should be Federal siting of electric lines that is analogous to the siting under section seven of the Natural Gas Act.

Mr. SAWYER. Thank you very much. I appreciate your flexibility, Mr. Chairman.

Mr. BARTON. The Chair is turning the Chair over to Mr. Largent, and the Chair recognizes Mr. Largent for 5 minutes for questions.

Mr. LARGENT [presiding]. Thank you, Mr. Chairman.

I want to ask your question, first of all, to a distributive generator, and that is Mr. Casten with Trigen.

One of the questions our chairman has been asking is about this 50 megawatt language that is in the bill and what would be an appropriate number.

You are a distributive generator. What would be a fair number if it was something less than that?

Mr. CASTEN. I believe that you should eliminate the number and describe what it is you are protecting. You cannot get a right number.

What I would suggest is that a distributive generation facility be defined as one that is designed and primarily used to provide electricity to its host, and that if you are doing that you have the right to an interconnect that is a standard and that is safe, but it is equitable for the size differences between things, because that is——

Mr. LARGENT. Is there a certain size, Mr. Casten, that has to be interconnected to a transmission versus a distributive distribution system?

Mr. CASTEN. Yes, there is, but it is going to vary by utility by utility, and I think Congress shouldn't get anywhere close to the electrical engineering. We can work that out. But the point is that if you can connect to the local distribution system you ought to have the right to do it if primarily there to provide services for that entity.

Mr. LARGENT. Okay.

Mr. CASTEN. Coming back to the earlier question, I think everybody is focused on a view that the world will continue to generate its power centrally and it will all go through the transmission system. I predict that the big competitive force will be transmitting energy through gas pipelines, oil trucks, coal, and it will be made at the other end of the line, and that is what will put the pressure on the transmission lines to behave.

Mr. BARTON. Will the gentleman yield just to follow up on that?

Mr. LARGENT. Sure.

Mr. BARTON. We thought about a functional definition instead of a discrete number, and the reason we do not have a functional definition is that we are told that there are some fairly creative utili-

ties out there and distributive generators that can game that definition.

Are you satisfied that there are attorneys adequate enough to the task to come up with a functional definition that can withstand the gamesmanship?

Mr. CASTEN. I am reasonably satisfied, and we will submit the best shot we can that would do that. The gaming is severe right now.

Mr. BARTON. Okay. Thank you. Thank you, Mr. Largent.

Mr. LARGENT. Let me ask Mr. Kanner, Marty, I want to ask you a question about the remedies for market power. If FERC had ability to address—market power, does it have to be divestiture? That is the first question. Or does divestiture have to be one of those tools that they have in their box?

No. 2, if you say it does need to be in the tool box, does it have to be permanent divestiture?

And then, three, because most people have viewed the market power issue as being sort of transitional, maybe over a 3- to 5-year period of time, does the potential exist to say that we could sunset FERC's ability to address market power after, say, a 5-year window?

Mr. KANNER. Thank you, Congressman. Those are all very important and valuable clarifications.

We do not advocate forced divestiture of all utility generation. It is simply not real. And we do think that it is a useful tool, as a tool of last resort, but there are many other things that can be used. I note that in the State of Texas, where they do not prescribe asset divestiture, they do have a system where the utilities, in essence, auction off the capacity from generation, or some portion of it, for a set period of time, and I think that is a very effective tool to both foster the competition that we need and address market power. So it is sort of a "twofer" if you will.

And I think that, as they did in Texas, some of those remedies can, in fact, be sunset. I would urge the committee, while we have our ideal language that does grant FERC that last resort mechanism of divestiture, that the Texas model is also a very valuable one for the committee to look at.

One of the keys there is that the utility, itself, prescribes its mitigation plan, as you did in the bill that you offered with Mr. Markey, so the utility says, "Here is what we propose to do," and then the Commission reviews whether it is adequate, and the bill can prescribe what some of those tools can be.

Mr. LARGENT. Okay. The Chair is going to give himself 1 more minute, since the chairman took some of my time, and I wanted to ask Ms. Moler a question.

I think Mr. Sawyer talked about the analogy that you used between what we did—and I wasn't here, unfortunately, which is why I ask the question—the analogy between gas transportation and what we are attempting to do in terms of regulating the transmission lines and not having, you know, the FERC regulate unbundled retail sales and States regulate bundled sales.

How did that work with gas and how do you see—I mean, can you kind of enlighten us on that analogy a little bit?

Ms. MOLER. The very short course in the evaluation of the natural gas rulemakings would go something like: first, FERC tried to have some special programs where you could have customer choice if you wanted it. They were reviewed by the courts. They were found to be discriminatory. FERC then eventually, in Order 636, required all gas pipelines to develop tariffs that would provide open access, same terms and conditions for everyone, use the gas pipeline, and also required the sale of the natural gas to be separated from the transmission as far as the corporate arrangement is concerned.

It did not go beyond the city gate, so a lot of States still have bundled sales, so it is possible to have both bundled and unbundled transmission subject to the same rules as far as the interstate aspects of it are concerned.

And the gas market has been relentlessly competitive since that time.

Mr. LARGENT. Okay. I am going to yield to the next questioner, but I would like to get maybe a 1- or 2-page summary of what you just said, and maybe a few more details on that, if you would not mind.

Ms. MOLER. I would be happy to do so.

Mr. LARGENT. Thank you.

Who is next? Ms. McCarthy from Missouri?

Ms. MCCARTHY. Thank you, Mr. Chairman, and thank you for your generous use of time. I hope that we can all be granted the same.

I wanted to begin, first of all, by welcoming back Mr Casten. When you visited with us the last time, as we were having discussions about what would be in the perfect bill, you mentioned to me that there are, in fact, at least in our State, and perhaps in others, laws that impede companies from competing, and you were very enthusiastic about us taking up and passing a bill.

But does this bill that we are looking at, if it were enacted as it is currently drafted, really solve or exacerbate problems you are facing in trying to conduct your business today in Missouri? And I would like any other panelist to reflect on that, as well.

And I would like to ask a second question to you, Mr. Casten, to Mr. Cooper and Cowart, and that is one that I asked an earlier panel today. Does the Barton bill provide sufficient guarantees that renewable power providers will be able to compete successfully in a deregulated market, and would it, indeed, improve reliability in a restructured market?

Mr. Casten, thank you again. I am quite proud, as is my county executive, of the work you are doing. In fact, she was just in New York on a national panel that "Forbes Magazine" sponsored talking about the public/private partnership that you have established in our community. It is a great model to us all.

But my concern, as a member of this committee, is to make sure whatever we do at the Federal level enhances that, does not impede it, and, therefore, speaks correctly to it.

Thank you.

Mr. CASTEN. Thank you for the question.

There are a series of barriers that we face that I wrote about in chapter eight of my book, and I am not sure how many of them you

can deal with at the Federal level, but I will just take off some of the ones that are there.

Fifteen States make it illegal for a third party to generate power, and I think that the Federal Government in the bill could say everybody can generate power.

There is a law in Missouri, as you know, that is an anti-flip-flop law which has been used that if you have once been supplied by one supplier, you cannot flip to another one. That is a pretty effective way to shut off competition, and that needs to be affirmatively stated.

The largest problem that distributed power faces is interconnection, and it is a boring electrical engineering thing, and I appreciate the panel dealing with it, but it is consistently used to say, "We have got to have these safety standards that are appropriate for a 1,000 megawatt nuclear plant apply to everything that comes on line." As the chairman of the West Chester Putnam Boy Scouts, we are trying to put in a 12-cabin campground that is sustainable, and we want to put up 12 kilowatts of photovoltaic, and the local utility has been given the right to force us to spend $30,000 testing the interconnect. They have no standards.

Well, you have got net metering in the bill, but if you do not get the interconnect standards set by an impartial agency, then net metering won't help.

So get the interconnect. I do not think that you can get one bill that does everything the first time. I think you have done a great job as far as you have come. It can be improved, of course. But get it started, and then, with 2 years in, come back and fix up some other things.

Your second question was: does it give enough help to the renewables?

Ms. MCCARTHY. To compete successfully.

Mr. CASTEN. To compete successfully.

Ms. MCCARTHY. And provide reliability.

Mr. CASTEN. Okay. I think that it gives enough with the interconnect to take 2 years and see what happens.

I am struck by Fredrich von Hayek, who said that the affairs of human beings became so complicated that nobody could predict what they would do, about 30,000 years ago.

And so the minute you change the rules and open it up to competition, I am looking over my back, because somebody is going to figure a way to do it cheaper, and I think renewables will—see what happens for a couple years and then adjust it, is my advice.

Ms. MCCARTHY. Mr. Cowart?

Mr. COWART. All right. I will take my turn.

First, I would like to make an observation about distributed resources, generally. We tend to concentrate on distributed generation as an important goal, as an important public value as we move into a more competitive environment, and I agree with Mr. Casten that distributed generation can be a really important resource for the Nation.

But efficiency resources are also distributed. They are modular. They can be manufactured at scale. And they produce, in an electrical sense in terms of providing electrical service to end users, much of the same benefits as distributed generation.

We need to remember to support both distributed efficiency and distributed generation as we go forward.

To answer your question about renewables, I do not believe the bill does do enough to ensure the healthy future for renewables that the Nation will need.

With respect to reliability, as I said earlier in my remarks, I am very concerned, in fact, that we are missing the boat on reliability. We are leaving out of the equation here one-third of the picture—that is the efficiency with which electricity is ultimately used, which drives the problems that we are seeing in transmission and in generation adequacy.

And I know the question will be asked: well, why is that a Federal issue? Why is energy efficiency a Federal issue?

Probably 10 times today, maybe more, I have heard people say that reliability is a regional issue, that incentives ought to be given to support new transmission investments, and incentives need to be given to open up the market for the construction of new generation.

Because the grids that we all are connected to are regional in scope, the physics of those grids dictate that what happens somewhere else on the grid is going to affect reliability everywhere and the price everywhere. And, for that reason, it just doesn't make—it is not logical, and we are leaving a lot of money on the table if we say that an RTO or other reliability organization has the authority to mandate the construction of new transmission for reliability purposes, or we can raise the reserve margin across an entire region for reliability purposes, which are going to raise costs to everybody.

But we do not have a mechanism at the regional level to support enhanced investments in energy efficiency which could achieve the same reliability goal less expensively.

Ms. MCCARTHY. Mr. Chairman, I know that time has expired, but I know there are a couple of other panelists who would like to speak to the reliability question that I raised. May I have an extension of time?

Mr. LARGENT. The gentlelady has had an extension of time, but yes, if you would like to have one more response, that would be fine.

Ms. MCCARTHY. Yes. Mr. Segal, I think you wanted to speak, and then Mr. Cooper.

Mr. SEGAL. Thank you, Congresswoman.

Ms. MCCARTHY. Or whomever.

Mr. SEGAL. It will be a real short answer for us.

We are not here to talk about the renewables portfolio or anything like that. As service contractors, the bottom line is this with respect to what is in the bill: the bill has a good first start in some areas with respect to open books and records, but, frankly, that is not much of a start.

In order to actually fix the problem with respect to cross-subsidization, getting into unregulated affiliate markets, there need to at least be broad principles articulated within the bill, as there were in earlier drafts. There need to be broad principles that include a clear prohibition and cross-subsidization, because, just like this committee recognized in the Telecommunications Act of 1996,

there are not sufficient protections in existing antitrust law with respect to competition in unregulated markets. There need to be at least some mechanism to make sure that these small businesses—really, the small business discussion item for this bill, these small businesses do not fall through the crack because there is no enforcement mechanism in place to make sure that they are not crushed by utilities as they try and move into unregulated markets.

Ms. MCCARTHY. Mr. Smith?

Mr. LARGENT. Maybe we can have the rest of the panelists submit their responses in writing. We have got to move on. There is a reception in here at 4, I am told, so we have to keep moving.

Ms. MCCARTHY. First things first.

Mr. BARTON. The gentleman from Illinois, Mr. Shimkus, is recognized for 5 minutes.

Mr. SHIMKUS. Thank you, Mr. Chairman.

Mr. Kanner, will you please describe for me horizontal market power? Just define it. I am having a hard time getting it defined the last couple days. Can you do that?

Mr. KANNER. Sure. It would be where, in a given market all trading the same thing or selling the same thing, the ability of an entity or a group of entities to raise and sustain prices above what would occur in a competitive marketplace.

So, in other words, if it is office supplies, I could sell pencils for whatever I want and there is no one else that can effectively cut my ability to do so.

Mr. SHIMKUS. And so, in the term of power instead of office supplies, it would be controlling the price?

Mr. KANNER. In terms of power, it would be two summers ago in California where the generators in southern California were able to raise the prices 3,500 percent in some of the ancillary services market and sustain those prices because there were only four players.

Mr. SHIMKUS. Why cannot a quality, independent RTO approved by FERC, which, based upon my understanding, would require open access, why can they not control or mitigate this type of market power?

Mr. KANNER. Again, in California during those price spikes there was a qualified ISO approved by FERC in place, and that entity went to FERC, went to a Federal regulator, to ask for help to resolve the problem.

You simply have markets that get defined by transmission constraints, and within those markets, if you do not have enough players, then you do not have the competitive price check that I think we are all looking for.

Mr. SHIMKUS. Ms. Moler, always pleased to see you again after attending so many hearings. Do you want to add to this for me?

Ms. MOLER. The only thing I would add to it, Marty—I believe that Marty, Mr. Kanner, has correctly described the answer to your market power question.

A qualified RTO can work if all transactions from all of the entities participating in the RTO have to be under the same rules. A lot of the RTOs that are already approved by FERC do not—the tariffs do not apply to utilities' sales, bundled sales to their own

customers, so they are first in line and they are not even on the tariff.

So they are a good start. Some of the RTOs would do that, I might add. But you have got to have all uses of the transmission system covered.

Mr. SHIMKUS. If the FERC required for the system to be open—and we are talking physics here—and people put power on the grid and the consumer pulls power down, it is in a pool, and so the producer has a record of how much they are putting on the grid, the consumer has a record of how much they are pulling down, and those interact, and if the grid is open, how is there horizontal market power?

We do not know where those electrons are going. That is my point.

Ms. MOLER. The electrons all get mixed up. Right.

Mr. SHIMKUS. I mean, that is the point. In the physics of this in this debate, we cannot follow it from the producer to the consumer. All we know is that it is going to a pool and people are pulling it down, and we are going to individually contract with a producer.

So if the FERC requires that the ISO or the RTO or the transco is opened, why doesn't this system work? People are telling me they need more tools than that.

Ms. MOLER. I believe that truly open access, where it covers all the transactions on that grid, is a very effective remedy for market power. I view that as a market power initiative.

When people talk to this subcommittee and advocate market power remedies, I believe that truly open access, as described in the amendment that we submitted today, would accomplish that.

Mr. SHIMKUS. And, Mr. Casten, do you want to just add to that debate on the physics?

Mr. CASTEN. The only point I would say is that the issue that people are concerned about came about because there was no price signal to the consumers, and so we want to be careful trying to solve a problem with legislation. We can get the wrong problem.

The consumers did not see that high price and could not do anything about it. Hopefully, in a competitive market consumers will say, "I do not want to pay $3,500 a megawatt hour right now. I will do something else." That will solve some of the market power from the other end.

Mr. SHIMKUS. As we saw with the price spikes in the midwest, there has been numerous entries now into the generation, or at least proposals on the board to fulfill the void.

Thank you, Mr. Chairman, for being so generous with the time, and I yield back the balance of my time.

Mr. LARGENT [presiding]. The chairman wants to announce that any and all members who have additional questions can submit those in writing for the panelists, and we will get responses.

I recognize the gentleman from Massachusetts.

Mr. MARKEY. Thank you, Mr. Chairman, very much.

One thing I have learned is I never get in between Steve Largent and a reception.

We are going to keep that consecutive game streak going here, you know what I mean?

You know, here is the thing that I try to keep in the back of my mind, which is that these are monopolies, you know, and it is a deep-seated pathology. Okay? It really is. And you are what you eat, and when you eat monopoly profits for that long it is going to be hard to change, and there is a kind of a paradox when you deal with monopolists, when you legislate in that area, which is that it takes more regulations to put on the book in order to break up the monopoly than already existed beforehand, but it is toward the goal of making sure that all the rest of these competitors can get in, and once all the competitors are in and secure then you can take all the regulations away and then you do not need any at all.

But breaking down 100 years of pathology is not easy, so you have got to go through that process to turn it into a healthy, balanced, normal marketplace, which most other parts of the economy have.

So what I would like to ask—first, Ms. Moler, I will try to get all my questions in to Ms. Moler and Mr. Kanner—is why is it that in the testimony today all the people representing retail consumers and industrial consumers and independent power producers and power marketers and other competitors have very serious problems with the Barton bill, the transmission, the RTO, the merger, and the other market-power-related provisions, and all the monopolies support the Barton bill?

Why is that, Ms. Moler? What, in your opinion, do you think it is about the Barton bill that——

Ms. MOLER. I would hazard a guess that they do not believe that the monopoly power has been appropriately constrained.

Mr. MARKEY. What do you think, Mr. Kanner?

Mr. KANNER. Well, Congressman, I think we can say that very clearly all of the proponents of markets and competition and consumers believe that Congress needs to and must address these sets of issues if we are going to receive the intended benefit to competition.

Mr. MARKEY. Okay. Now, Mr. Kanner and Ms. Moler, earlier one of the witnesses from the last panel mentioned some specific examples of instances in which incumbent utility monopolies had exercised market power, including Florida Power and Light, AEP, and some utilities in Wisconsin.

Are you familiar with any real-world examples of market power problems? Can you point to any States, regions, Mr. Kanner?

Mr. KANNER. I think you can. I used earlier the example in California, which is, to me, the starkest, where there were dramatic price increases in the ancillary services market of some 3,500 percent and it was limited there because the computer could only enter four digits, so it was $9,999. So that is a very clear example.

I think we have had market power examples elsewhere where these new generators that Mr. Shimkus mentioned are desirous of building new plants, but they are told that they are last in line because the utility's own plants get to grandfather and be cued up first for interconnection, and the longer you wait, not only do we forestall that competitive market, but the cost of interconnection, because of the impact on the system, goes up, and ultimately those projects can be uneconomic, not viable.

Mr. MARKEY. Mr. Cooper, could you give me the nightmare scenario? Could you briefly?

Mr. COOPER. Well, the nightmare scenario I think occurs in reality in California. If you think about what happened there, the State of California could not make a market on its own and had to turn to the FERC and say, "We need some relief." The simple fact of the matter is that this is an interstate market. The nearest competitive power may be across the State border, and the State cannot—the entity that has that power can, in fact, be operating in both States.

Imagine the screaming and shouting if the State of California tries to tell a generator in Nevada who is withholding his power in California that they have to sell it into the State. It cannot happen. They would just scream and shout and say they crossed the State border.

This is an interstate market. The transmission grid is a highway. This is the highway of commerce.

Imagine if you are a vegetable producer in Texas who says, "Look, let's put up a toll booth at the State border and turn back all the trucks that might come from California with fruit in them." This is a nightmare system.

You have to have a supply side, a demand side, and a highway of commerce in between, and clearly that highway is an interstate highway and it is an interstate market.

Mr. MARKEY. Ms. Moler, let me ask you a question.

Does section 101 of the Barton bill codify the 8th circuit decision which held that FERC cannot bar utilities from giving first priority in transmission to serving their native load even if this undercuts their obligation to provide firm transmission service to other parties?

Ms. MOLER. I believe that section 101 does codify the 8th circuit decision. The FERC——

Mr. MARKEY. And what impact does that have on FERC's ability to prevent utility monopolies to grant themselves preferential service for their own use and prevent others from fairly, effectively, and efficiently utilizing the transmission grid?

Ms. MOLER. FERC would have no authority to look at the bundled transactions that you describe.

Mr. MARKEY. None at all?

Ms. MOLER. Correct. The reliability provision does talk about FERC having authority over "bulk power facilities." And, as I said in my prepared statement, I cannot reconcile the bulk power sections and the jurisdictional sections.

I noticed that NERC today proposed to solve that by saying, notwithstanding any provision of the Federal Power Act, this reliability authority would be up and running, but section 101 does amend the Federal Power Act.

Mr. MARKEY. Thank you.

Thank you, Mr. Chairman.

Mr. LARGENT. Thank you.

I recognize the gentleman from Tennessee.

Mr. BRYANT. Thank you, Mr. Chairman.

Again, let me thank you for just continuing to hold these various hearings on this very important issue.

Today we have had two very representative panels, and I appreciate their testimony. Unfortunately, I have been in and out today with another subcommittee hearing with the Surgeon General in one, and also on the floor talking about health care, which is another very important issue, certainly one of the day.

In order to avoid duplication, since I have not heard all of your testimony, I am not going to wade in and try to ask you additional questions, but, Mr. Chairman, I would ask that we be given a few days and maybe we could submit questions in writing if we have any additional questions.

Mr. LARGENT. Yes. Without objection.

Mr. BRYANT. Thank you.

And, again, thank you for your presence here today.

I yield back the time.

Mr. LARGENT. And the gentleman from Texas is recognized for 5 minutes, Mr. Hall.

Mr. HALL. Mr. Chairman, thank you.

I have noticed that there are not very many people asking Mr. Smith any questions, and I left—I had to leave and go and come back, and I have been going to see where Mr. Markey was. He goes and comes and then come back revved up and ready to go.

Are you the same one they call "Smitty" down in Austin, Texas?

Mr. SMITH. Mr. Hall, I am that same Smitty.

Mr. HALL. The same one that came to my office and told me everything I was doing wrong——

Mr. SMITH. And hope to do that again.

Mr. HALL. Well, I enjoyed you. You are a class guy.

Mr. SMITH. Thank you.

Mr. HALL. And you just say what everybody else says, so—but I noticed that some here represent AARP, some Americans for Affordable Energy, coalition coordinator for Consumers for Fair Competition, Consumer Federation of America, and then you represent everybody else. You represent the public citizen, right?

Mr. SMITH. Right. That is what I try and do.

Mr. HALL. I have a quick question to ask everybody, but I will ask you first. How has this bill been implemented in Texas that we just passed there? How is it working?

Mr. SMITH. Well, it is good and bad and ugly, and the——

Mr. HALL. In that order?

Mr. SMITH. Yes. I think our Public Utilities Commission has done a great job of doing rulemaking on this.

The bad news is that we did not anticipate a number of the problems in the bill and we did not get language tight enough in a number of key areas, some of which you have been talking about today.

Mr. HALL. It was amazing to get a bill with the vote you got down there, right?

Mr. SMITH. Well, especially in the House. And it was a bill that was heavily worked, and we got tremendous—almost everybody, with the exception of Public Citizen and the consumer groups, were in support of the bill, and the chairman and the House did a tremendous job down there. And we got an awful lot in that bill. I do not mean to be belittling it. We just did not think that this was a good idea.

But the ugly part and the part that I think is really important here in this conversation is what we did not really understand was that the way we set up the ISO, the ball has been stolen from the Public Utilities Commission on a number of critical matters regarding reliability, access to transmission, the data collection about consumers and how consumers get shifted around.

And so when you all do your ISOs, unless you—our goal would be to have them done publicly, but if you do have these regional ISOs, make sure you have a significant majority of consumer representatives on those boards that control them; otherwise, the same big old boys that have been running the system are going to continue to control who gets access and you will continue to have monopolies really running the system.

Mr. HALL. Part of your presentation was to assure we are not just benefiting the big boys.

Mr. SMITH. Yes. That is the essence of it.

Mr. HALL. You recommended allowing communities to buy at wholesale for their citizens, and you said to help protect residential consumers you should consider adding a provision called "community choice." There is a provision on aggregation, but community choice you say is different. How is different from the provision the that chairman put in his bill?

Mr. SMITH. We had a robust discussion a few minutes ago about this, and——

Mr. HALL. Okay. I won't—if you have covered that, I won't go into it.

Mr. SMITH. But let me give you the short version, and that is that what happens then is the community gets together, votes on whether to create a new public power entity or buy power for its consumers, and then we think gets the wholesale deal.

In Texas, what we found was that when people went out to wholesale they were getting 20, 28 percent reductions in price. The best in the country right now, the best market in the country right now in Pennsylvania, the star market, it is only an 18 percent difference from what it was before they did deregulation.

We believe that wholesale gets you better deals for the average consumer, and that is the key message that we have got, so that is why we are suggesting that you give the community choice and then you give the people the opportunity to opt out if they would like to do so.

Mr. HALL. Are you for this bill?

Mr. SMITH. No, sir, I am not. As I mentioned earlier, I think it is a—there are a couple good things in it, but it needs to go further.

Mr. HALL. All right. You are not for the bill.

Mr. Brice, do you support this bill?

Mr. BRICE. With some revision.

Mr. HALL. All right. Betsy?

Ms. MOLER. With some change.

Mr. HALL. Do you all have the same opinion?

Mr. BARTON. I have seven amendments. By the time we are done with the amendments, it will not look like the original bill, that is for sure.

But we need legislation.

Mr. HALL. Who was it that asked a while ago and they gave us all the things that were wrong with it, and I whispered to the chairman, "Ask him what is right about that."

Mr. BARTON. That was our strongest supporter.

Mr. HALL. Well, you cannot fault this chairman. He has laid it out there and we can take shots at it and can restore it and correct it maybe. I hope we can.

Mr. Kanner?

Mr. KANNER. With some substantial changes, substantial.

Mr. HALL. Mr. Cowart?

Mr. COWART. Also with substantial changes. I think it can be restored, frankly.

Mr. HALL. Maybe I have not got enough time for you to tell me what. Go ahead. Go ahead and tell me. You are just against it like it is and you do not think it is repairable?

Mr. COWART. No. I said I think it could be repaired. There are some very significant, positive elements in this bill, and it is just the very important parts of what ought to be done aren't included at all.

Mr. HALL. Mr. Smith, you have already spoken. You have not changed?

Mr. SMITH. Have not changed in the last five witnesses.

Mr. HALL. Mr. Casten?

Mr. CASTEN. Given a choice between this bill and no bill——

Mr. HALL. You, in your testimony, seemed to have wanted a smaller bill. You think the time is not right, or something?

Mr. CASTEN. No, I did not mean that at all.

Mr. HALL. Did I misunderstand you?

Mr. CASTEN. Yes, sir.

Mr. HALL. Okay.

Mr. CASTEN. Given a choice between this bill and nothing, I wholeheartedly support passing the bill.

Mr. HALL. Okay.

Mr. CASTEN. I think there are some more barriers that have not been dealt with and they could be added, but you are in the right direction, sir.

Mr. HALL. Well, you know, we are at the subcommittee level and we will have a new chairman when we get to the committee. I do not know in whose hands and what those hands want to do with this bill when it gets there. And Rules is going to have an awful lot to say about it, the Speaker will have a whole lot of input at the Rules Committee, and when it gets to the floor—we are a long way from the bill. But I agree with you—I think it is better than no bill, and that with some real helpful amendments that we can maybe restore this vehicle.

Yes?

Mr. SEGAL. Mr. Hall, I have got good news and I have got bad news.

Mr. HALL. Give me the bad news first.

Mr. SEGAL. Bad news first is, as the bill is currently drafted, the service contractors cannot support it. But the good news is, all we have to have is a cross-subsidization provision in with broad principles and we can support pretty much any other bill, no matter

what it says about all their transmission problems, doesn't matter as long as there are good, broad principles on our issue.

Mr. HALL. To get that one thing, how many votes up here can you deliver?

Mr. SEGAL. I will answer that question. We have chapters in every Congressional District in every State, air conditioning contractors, alone, 4,000 of them, and we will mobilize——

Mr. HALL. It is already getting to be winter now. How about the people in the wood business?

Have you got any people——

Mr. SEGAL. Electricians, plumbers, you name it, they are going to kill me because I am leaving somebody out, but every service contractor that is facing unfair monopoly based competition, we are absolutely willing to support a bill that contains adequate provisions on cross-subsidies.

Mr. HALL. Mr. Chairman, I asked to be last because I wanted to go out in good nature and real gratitude to you, and I say this in all sincerity, for the openness, that your door has absolutely been open to everyone, and you have traversed this Nation back, forward. I have asked for hearings in Honolulu. You have turned those down. I did not like that.

But I think that we owe you a great debt of—hell, I am the only one up here.

I am in slapping distance, so I have to be for him.

We do thank you for the way you have engineered this, and I am honored to be a part of it with you.

I yield back my time.

Do you want me to take another 30 minutes?

Mr. BARTON. No, no. I think we are—we were supposed to have been out of the room at 3, because they are getting ready for an Armey reception at 4.

Let me close the hearing. I want to thank you, Congressman Hall. You have been polite to me. This is a team effort, and I could not ask for a better ranking member than you in terms of being open and congenial and forward-thinking in trying to reach the goal.

I want to compliment the full committee ranking member, Mr. Dingell, for all of his accessibility and his willingness to listen and make sure the process goes forward.

Chairman Bliley has been very supportive of the hearing process and moving toward delineation of the issues. So it is a team effort.

I want to thank this panel. I apologize. Because of the lateness of the day and the votes, we did not have all of the subcommittee back to hear your testimony, but it is in the record and we are going to be looking at it.

As I have told this first panel, my intention is to go to markup the week after next, so, Mr. Casten, who said he had some language on functional distribution, we need to look at that, and I know Mrs. Moler's group has got some discrete language. I know Mr. Kanner's group has. Try to get a champion on each side of the subcommittee to bring it forward. I am going to sit down with Congressman Hall as soon as we get all that in, go through and see if we need to change the current draft before we go to markup, or

whether we want to go to markup and then have a log of amendments. But we are going to have an open markup process.

The one thing that I am going to discourage is subcommittee members coming into the markup having not shown their amendments to anybody. I cannot prevent that from coming up for a vote. It is an open process. But I am going to tend to be very negative on amendments that have not been shopped and have not been shown to both sides of the aisle in terms of them being accepted into whatever the legislative vehicle is.

Our subcommittee is well versed in the issue, well educated on both sides of the aisle. This is a big, big issue. I think it dwarfs telecommunications. I think it is more complex than natural gas deregulation was. So we need the best minds working on these issues, giving us the legislative language, and then I have got confidence, between the kinds of members we have on both sides of the aisle that are dedicated to trying to get a good bill, we can come up with a good bill.

I do not disagree with most of your testimony, quite frankly, that this is—you know, not too many of you are categorically for the bill as it is, but with some changes. The key is going to be, you know, how do we balance those changes in the good for the country.

I have told the republicans on the subcommittee when we meet, "I want suggestions on good public policy," and then we are going to have to make some political decisions, but I want suggestions on good public policy so that, if we start with good public policy, when we have to make a political decision to get the votes, at least the base underline is good public policy.

So I know you have got interest groups and I know your interest has got to be preeminent in your presentation, but when you go back and make your reports tonight or tomorrow to the trade groups that you represent, try to get them to think about not just what is best for you, but what is best for good public policy, because we have got a chance in the next 2 weeks to mark up a bill that restructures an industry that has never been in any type of a competitive market for over 100 years, and that is a real opportunity, and we ought to take advantage of it in this session of Congress.

I thank this panel. You are adjourned, and the committee is adjourned.

[Whereupon, at 3:20 p.m, the subcommittee was adjourned, to reconvene at the call of the Chair.]

[Additional material submitted for the record follows:]

RESPONSES OF DAVID K. OWENS, EXECUTIVE VICE PRESIDENT, EDISON ELECTRIC INSTITUTE TO QUESTIONS OF HON. JOE BARTON

Question 1. Some witnesses suggest including Clean Air Act amendments in electricity legislation based on the Waxman bill (H.R. 2900) or the Pallone bill (H.R. 2569). What is your position on these bills?

Response: EEI does not support including Clean Air Act amendments in electricity restructuring legislation. Any provisions affecting air emissions from electric generating sources should be part of an overall reauthorization of the Clean Air Act which applies to all industries, rather than done piecemeal in other legislation. Electric generating plants already face uncoordinated, overlapping and inconsistent programs under the Clean Air Act, probably the most complex of environmental statutes. Adding more requirements outside of the Clean Air Act structure would only make matters worse. Additionally, the air emissions included in both the Waxman and Pallone bills are addressed in the existing Clean Air Act, and implementation

of the statutory programs is underway or currently under development. It would be premature to add other requirements outside of the Clean Air Act before all the existing Clean Air Act provisions are fully implemented and the impact on overall air quality fully realized.

Question 2. You assert FERC has no authority over holding company mergers. If so, why did AEP and CSW submit their merger for FERC approval? Do you expect PECO Energy and Unicom to submit their merger for FERC approval? H.R. 2944 does not expand FERC regulation if it merely clarifies existing authority.

Response: The Federal Power Act does not grant FERC explicit authority over mergers of holding companies. In fact, FERC's assertion of jurisdiction over holding company mergers is relatively recent. Many disagree with its position as a matter of law. But, as a practical matter, litigation of this issue during the pendency of a merger could delay merger approval for years. Approvals of utility mergers already take too long. Thus, as a practical matter federal restructuring legislation needs to resolve this issue, just as it should resolve other issues where FERC jurisdiction is ambiguous. However, we are opposed to expansion of FERC merger authority over holding companies.

Question 3. Mr. Rao proposes establishing a rebuttable presumption that nonradical lines in excess of 60 kilovolts are transmission facilities. What is your reaction?

Response: FERC's seven part test, which is accepted in the Barton bill, properly concludes that a variety of factors need to be considered to correctly distinguish transmission from distribution. FERC developed this test in Order No. 888 after considering comments from all interested parties. FERC concluded that no single factor, not even voltage, is sufficiently important to be a primary measure of the nature of a given facility. Under the current FERC approach, FERC will give great deference to state determinations applying the seven part test. Mr. Rao's approach might well deny states authority over facilities that really serve a distribution function.

Question 4. Mr. Rao gives examples of IOUs redesignating transmission as distribution in order to avoid open access requirements. Why did Commonwealth Edison reclassify 40% of its transmission as distribution? Why did Wisconsin Public Service Company try to reclassify over 90% of its transmission as distribution?

Response: Every proposal to clarify what is transmission and what is distribution is subject to regulatory review and approval by state regulatory commissions and FERC. FERC established the seven part test for identifying transmission facilities in Order No. 888 because it recognized that restructuring could require utilities to revise precisely how they accounted for transmission and distribution facilities based on whether or not an asset was actually being used for a transmission or distribution function in a competitive context. FERC recognized, for example, that open transmission access could utilize facilities which utilities had traditionally treated as distribution for accounting and regulatory purposes. The requirement of open access distribution in state restructuring plans similarly could cause utilities to take a new look at how they classified various facilities. In fact, states such as Illinois have required utilities to refunctionalize as part of their restructuring legislation.

In Order No. 888 FERC also described the process and factors it would use to review these classifications. This process provides for public input, and deference to state determinations about the proper classification of transmission and distribution facilities within each state. However, FERC makes the final decision on all of these requests. No utility can unilaterally transfer facilities from one category to another. In short, this process is a natural response to the changing use and regulation of the utility delivery system that is fully regulated by FERC and the states.

Question 5. You state Congress should authorize States to impose reciprocity, which would give States the power to regulate interstate commerce, by denying out-of-state electric suppliers access to their retail markets. Are you concerned States may abuse this power? For example, New Jersey could use its reciprocity power to deny the access of coal utilities to its retail markets.

Response: With the modification we suggest, the only criteria which a state could use to require reciprocity involves whether a utility has applied for or provides open access distribution. A state could not impose environmental or other restrictions under this reciprocity approach.

Question 6. You state TVA provisions "absolves TVA of the most basic regulatory constraints." Under the status quo, TVA is not regulated, it has a closed transmission system, it sets its own transmission rate and power rates, Federal law requires its customers to buy from TVA, and antitrust law does not apply to TVA. H.R. 2944 opens TVA's transmission system, provides for FERC regulation of TVA transmission and power sales outside the region, gives TVA customers a choice, and applies antitrust law to TVA. What is a better deal for TVA, the status quo or H.R. 2944?

Response: The phrase you quote in your questions refers to Section 612 of H.R. 2944, which says that Subtitle A "shall be interpreted and implemented in a manner that does not adversely affect bonds issued by the Tennessee Valley Authority." We believe that this extraordinarily broad loophole virtually voids many of the regulatory provisions that might otherwise apply to TVA under other sections of H.R. 2944.

We also do not believe the goal of fair competition is advanced by allowing TVA to carry its subsidies and exemptions over the fence into competitive wholesale markets. If TVA is to be an active competitor in the electricity marketplace, it should play by the same rules as other active competitors.

RESPONSES OF ALAN RICHARDSON, EXECUTIVE DIRECTOR, AMERICAN PUBLIC POWER ASSOCIATION TO QUESTIONS FROM HON. JOE BARTON

Question 1. You say H.R. 2944 eviscerates FERC jurisdiction over the transmission system. That is not what FERC told us yesterday. FERC told us H.R. 2944 codifies Order 888. Let's be clear what you are asking for—you want Congress to go beyond Order 888 and give FERC jurisdiction over a larger part of the transmission system than it assessed in Order 888. Isn't that correct?

Response. APPA's view is *not* that H.R. 2944 eviscerates all FERC jurisdiction over the transmission grid. Rather, as I testified previously:

> [I]n attempting to create a bright line distinguishing Federal and State regulatory jurisdiction, two provisions of H.R. 2944 combine to eviscerate FERC jurisdiction over *significant components* of the interstate transmission network.
>
> Section 101(b)(1)(B) does not allow FERC regulation over bundled retail sales of electric energy. Section 101(e) allows for a FERC determination of whether a particular facility qualifies as transmission or distribution, but requires FERC to give deference to State commission decisions. When these provisions are combined, this section cuts FERC out of the regulation of *significant amounts of transmission access and use over bundled sales.* If this section is interpreted to allow a preference for bundled firm load over unbundled firm load on the same transmission system under emergency situations, then it is clearly inappropriate. Such an interpretation would undermine the goals of promoting competition and standardizing regulation of the national grid. [emphasis added]

The bill's attempt to establish a bright line between state and federal jurisdiction is likely to balkanize the grid and to lead to protracted litigation of the new divide. As private power companies seek to protect themselves from competition, they could use the extension of slate jurisdiction over facilities and the bright-line prohibition on FERC inquiry into the comparability of bundled retail service to unbundled wholesale service to establish effective barriers to competition.

Section 101 will prompt utilities to forum-shop, seeking to transfer assets to state jurisdiction where the regulatory climate is favorable and the objective is to protect their generation and merchant functions from competition.

APPA does not seek to extend direct FERC authority over the transmission of electric energy, as part of a bundled retail sale. However, the Commission must have the authority to ensure that all users of the transmission grid receive comparable, non-discriminatory access to the grid, whether the sale is characterized as a bundled retail sale, an unbundled retail transaction, or a sale for resale in interstate commerce. Chairman Hoecker has in fact sought just such a clarification in his testimony, illustrating that H.R. 2944 in fact does not codify Order 888. Rather it constricts the scope of the Commission's existing jurisdiction.

H.R. 2944 here raises two issues of grave concern to APPA. First, if transmission facilities are refunctionalized to "local distribution," it becomes much more difficult to make the case that such facilities must be controlled and operated by RTOs. The results may be RTOs that lack operational control over the entire bulk transmission grid. An RTO's ability to perform each of the functions identified by FERC and those identified within H.R. 2944 would clearly be impaired if, for example, a major portion of the grid's Available Transfer Capability, is controlled not by the RTO, but by local utilities. Of equal importance, an RTO's ability to expand the grid in response to the needs of all transmission customers will be hobbled by dependence on each local utility to upgrade non-RTO facilities.

Second, the bright line between bundled retail and unbundled FERC-jurisdictional transactions would appear to foreclose inquiry by FERC (or by a wholesale customer in a court of competent jurisdiction) into the comparability of the transmission services afforded by a local utility to its bundled sale retail customers in comparison to the rates, terms and conditions of transmission access afforded to wholesale transmission customers. One must remember that none of the independent system opera-

tors now in operation or the RTOs now envisioned by the industry intends to operate the entire grid—from generator busbar to customer meter. Thus, comparability of the wholesale and retail delivery services provided by the local utility is still an issue of great concern to public power. For the most part, APPA members are interconnected at sub-transmission voltages through facilities that may or may not be operated by RTOs. Thus, our members will remain subject to discriminatory conduct by private power companies. Reliance upon state Commissions to ensure that public power systems receive comparable access would result in increased regulation, as states are forced to take on functions now performed at the federal level. In addition, one can anticipate a proliferation of differing regulatory regimes among the states governing local transmission access. While each state properly must design and implement its own program for retail choice, standardization of the rules for local transmission access under a FERC-jurisdictional tariff is essential for the creation of large and liquid regional power markets.

Question 2. One thing we have heard loud and clear the past four years is the need to respect the States. You propose granting FERC jurisdiction over transmission used to make bundled retail sales. What is the position of the States on this issue?

Response. APPA has been among those urging Congress to respect the rights of the States (and their political subdivisions) regarding if, when and how to address retail competition. In our view, they, are better positioned than Congress to address these issues. This is why we have consistently, opposed a "date-certain Federal mandate" for retail competition. At the same time, we have endorsed Federal legislation to sort out the difficult jurisdictional issues necessary to make wholesale competition (competition in interstate commerce) work as intended, and to lay the foundation for effective retail competition in those states that have or may in the future proceed down that path. Theoretically, every electron in the grid flows in interstate commerce. We have never suggested that Congress could not endorse this expansive view of what constitutes interstate commerce, only that it should not. The problem then is how to draw reasonable boundaries between those issues subject to FERC jurisdiction, and those that should be left to the States. Transmission has historically been used to define the boundary, and, following Order 888, this has given rise to questions regarding FERC jurisdiction over transmission for bundled retail sales and unbundled wholesale sales. We believe that there should be comparability with respect to access, use and price for transmission services without regard to whether the facilities are used for bundled retail sales or unbundled wholesale sales. We believe this was one of many goals of Order 888.

Congress should make it clear that FERC has full jurisdiction over all elements of transmission in interstate commerce, including the use of subtransmission and distribution voltage facilities that are needed to accomplish the transmission of energy at wholesale. To the extent that the Congress determines that the states should retain jurisdiction over the transmission portion of bundled retail sales, Congress should also find that such jurisdiction is shared with the Commission. Where there is a conflict between state commissions and FERC under the Federal Power Act, the interests of the state should give way to the extent that they create a barrier to interstate commerce.

If we do not have uniform treatment of transmission facilities there will be wide disparities in treatment of similarly situated customers. For example, citizens of State A served by a publicly owned electric utility that purchases power at wholesale and unbundled transmission service from a private power company could be treated differently from other citizens in the same state who are retail customers of the same private power company simply because the IOU's transmission costs are bundled together with the power and distribution components of the retail bill. The opportunities for discriminatory treatment with respect to transmission access, use and charges in such situations are apparent.

We do not speak for the States on this issue, and therefore cannot provide a definitive answer regarding their position.

Question 3. You oppose FERC deference to the States in determination of transmission and distribution facilities, which is the approach FERC laid out in Order 888. Is FERC giving too much deference to the States? Can you give examples? You indicate utilities are trying to reclassify facilities. Is FERC agreeing to this reclassification?

Response. In Order No. 888, the FERC announced that it had jurisdiction over all facilities necessary to complete a wholesale transaction, without regard to whether such facilities were labeled "transmission," "distribution" or "local distribution." The Commission stated that it would apply a seven-factor test to determine what facilities were "distribution" facilities for purposes of determining the federal/state

jurisdictional split when a sale is made to a retail end user and that it would defer to state regulators' determinations of what facilities are distribution.

In the real world, under the guise of applying the seven-factor test, owners are seeking to "refunctionalize" (reclassify) substantial amounts of their existing transmission facilities in an attempt to remove these facilities from FERC jurisdiction. As of yet, the states and FERC would appear to have properly applied the seven-factor test. Recent utility initiatives give us great pause, particularly in light of the language proposed in H.R. 2944.

In one recently filed application to the FERC, a major transmission owner in Illinois has proposed to refunctionalize approximately 40% of its total transmission facilities to distribution. Although details in the filing are sketchy, it appears that almost all 138 kV and below facilities would be "distribution" facilities if FERC approved the application. Only 345 kV and above facilities would remain transmission.

Another transmission owner in Wisconsin submitted a filing to its state regulatory agency under which only 124 out of a total of 1,474 pole miles of existing transmission should remain transmission. The remaining 1,350 miles would be reclassified as "distribution." The filing would have left only seven of the owner's 33 interfaces available for transfer to a RTO.

In Order No. 888 FERC has stated that it will defer to state commission determinations. While such deference may be appropriate in the determination of what facilities constitute "local distribution" or "transmission" facilities, these proceedings do not take place in a regulatory vacuum. Restructuring presents many states with a substantial loss of regulatory jurisdiction to FERC (in the area of RTOs and transmission), to a self-regulatory NAERO (in the realm of reliability), and to largely unregulated markets (in the area of generation and marketing). State regulators will have a strong incentive to capture jurisdiction, by extending their purview from local distribution to the transmission of electric energy, even where such transmission is of an interstate or multi-state character. Owners also have a strong incentive to retain control of such facilities rather than transferring them to an RTO.

The refunctionalization of facilities from transmission to distribution raises significant issues, including:

- Would refunctionalization of transmission to distribution mean that FERC has no jurisdiction over these "distribution" facilities?
- Will these "distribution" facilities become subject only to state jurisdiction?
- Will operational control of these "distribution" facilities be transferred to the RTOs as originally planned or will owners retain full operational control over such facilities?
- Will these "distribution" facilities no longer be subject to the requirements of Order No. 888?
- Will these "distribution" facilities no longer be subject to any of FERC's open access or comparability requirements?
- Will state regulators determine rates, terms and conditions under which wholesale customers have access to these "distribution" facilities, including whether owners can reserve significant portions of the capacity of these facilities for reliability purposes (i.e., CBM), impose load ratio restrictions on the use of such facilities, adopt non-comparable allocation or curtailment schemes or otherwise impose rates, terms or conditions that would discriminate against and limit customer access to such facilities?
- Will states that have different or conflicting economic interests use their new authority to balkanize regional markets, e.g., to prevent the transmission of low-cost energy to "downstream" states or to prevent the transmission of energy deemed to be insufficiently "green?"
- Will customers be exposed to a vertical rate pancake if they are served by "distribution" facilities or are purchasing from a generator connected to the grid by "distribution" facilities? If so, will the sum of the vertical pancake exceed the owner's current transmission rate?

The functional approach to differentiating between transmission and distribution facilities makes sense, so long as it is applied taking into account these and other questions. It is appropriate for FERC to consider state commission determinations, but requiring FERC, by statute, to give due deference to state commission determinations at the very least is an invitation to litigation.

Question 4. Mr. Rao proposes establishing a rebuttable presumption that non-radial lines in excess of 60 kilovolts are transmission facilities. What is your reaction?

Response. A rebuttable presumption based on the size of the facilities as proposed by Mr. Rao would be appropriate. We have not addressed what the appropriate threshold should be.

In light of our concerns with the refunctionalization of transmission facilities to local distribution, we agree that a lower voltage threshold provides greater assurance that utilities will not be able to create barriers to competition. A rebuttable presumption would also allow a transmitting utility to petition for the exclusion of specific facilities or classes of facilities from transmission.

Congress might consider, for example, the restructuring legislation recently enacted in Wisconsin. According to The Energy Daily, Friday, October 8, 1999, page 2, Wisconsin's Reliability 2000 legislation contains language that classifies anything above 130 kilovolts as transmission and puts the burden on a utility to explain why lines in the 50-130 kilovolt range should not be classified as transmission.

Question 5. You say "it is difficult on public policy grounds to sustain the proposition that publicly owned transmission facilities should be subject to FERC jurisdiction." I agree that small public transmission systems should be exempt from FERC jurisdiction, and H.R. 2944 does that. Why should large public transmission systems like New York Power Authority be exempt from FERC regulation? Why shouldn't these large systems be fully open?

Response. As noted in our testimony, APPA appreciates the fact that H.R. 2944 limits FERC jurisdiction over small publicly owned transmitting utilities. The specific comment in our testimony, that is quoted in this question is based on a number of factors. For example, most of the large public power systems that own substantial amounts of transmission facilities have voluntarily filed tariffs with FERC or a Regional Transmission Group that provide for comparable transmission service, are participants in ISOs (such as is the case with the New York Power Authority), or both. The transmission facilities of these utilities are fully open. In addition, publicly owned transmitting utilities are subject to FERC open access transmission orders under amendments to the Federal Power Act contained in the Energy Policy Act of 1992. Further, APPA supports the expansion of FERC authority to require all transmitting utilities to participate in RTOs. However, as noted and more fully explained in our testimony, the exercise of this authority with respect to publicly owned utilities *must* take into account the unique conditions and characteristics of publicly owned utilities. Therefore, based on what publicly owned utilities have already done to provide comparable treatment, what they may be required to do on a case-by-case basis under provisions of the Energy Policy Act of 1992, and what we believe should occur with respect to RTO formation and participation, additional FERC jurisdiction appears unnecessary. However, to the extent Congress concludes that FERC jurisdiction over publicly owned transmitting utilities should be expanded, we urge that such regulation be as light-handed as possible to ensure comparability without imposing unnecessary regulatory burdens.

Question 6. You want to limit FERC regulation of large public transmission systems to non-rate terms and conditions. If large public systems retain rate authority, they could shift power costs into transmission rates, and would have an incentive to shift costs if their power costs were above-market. Should publics be able to shift power costs into transmission rates?

Response. Shifting power costs into transmission rates is inappropriate. For the reasons set forth in our testimony, we do oppose FERC jurisdiction over public power transmission rates. jurisdiction over rates and revenue requirements should be limited to ensure comparability. Comparability encompasses standards of reasonableness and non-discrimination. We stated in our testimony that "where FERC determines that rates are not comparable *or are discriminatory,* it could remand the rate to the local regulatory authority for review and revision as necessary. Public power systems would therefore retain local control over rate making and revenue requirement decisions." [emphasis added]

Question 7. You say market power issues "simply cannot be addressed by the individual States." Did California reduce generation market power? Did the New England States reduce generation market power? Did Texas reduce generation market power?

Response. In fact, the states have a major role to play in the control and mitigation of market power, through the conditions and directives they impose on utilities during the restructuring process. States, for example, have used utility generation divestiture to ensure there are multiple owners of deregulated generation assets within their state. Without such state action, their restructuring efforts risk the creation of unregulated monopolies.

Once the divestiture has occurred, most states will find it difficult if not impossible to mitigate market power, because electric power markets generally extend far beyond the boundaries of a single state. Texas, with its DC voltage interconnections to other states, is, like Alaska and Hawaii, an obvious exception. Even a state as large as California is overwhelmingly dependent on electric power imported from other parts of the west. In fact, throughout much of the year, imports set the mar-

ket price for power sold into the California market. Thus, concentration in the electric generation market in a region, particularly where coupled with control of scarce import capacity, presents a risk from the exercise of market power in these "downstream" markets. If the concentration is in the upstream (and out-of-state) region, regulators in downstream states have few if any tools to deal with such concentration.

States lack the power to halt the trend of mega-mergers intended to create large, regionally dominant generation suppliers. Neither can the states effectively halt the creation of multi-state holding companies whose complex financial and business relationships are difficult for even federal regulators to decode. This problem will become even more serious if the current restrictions on the scope and configuration of utility holding companies are eliminated by the repeal of the Public Utility Holding Company Act.

Question 8. Should individual States have the authority to establish transmission reliability standards? Would fifty different state standards improve reliability? What would be the impact on interstate commerce?

Response. States have had the authority to regulate the plans and actions of the utilities within their borders with regard to reliability standards for several decades as a part of the voluntary industry self-governance system known as the North American Electric Reliability Council (NERC). The NERC system functions through several regional grids that really reflect the engineering of the system and have little relationship to state political boundaries. This system worked to produce the most reliable electric system in the world while the industry functioned through the geographic monopolies regulated primarily at the state level.

Since the passage of EPACT in 1992, when Congress opened up the national electric transmission grid to promote greater wholesale competition and exchange, those geographic borders have been become even less relevant to the control and flow of electricity around the country. The industry, with an unprecedented level of cooperation, decided that the voluntary system no longer fulfills the reliability needs of the system, and that a self-regulatory organization (NAERO) with federal enforcement powers was needed to provide the proper level of focus on the reliability of the system. This focus on national reliability standards is also needed to support the expected increase in market activity that will be carried out over the system.

There is nothing in the industry consensus language, which is included in H.R. 2944, that undermines the states' abilities to regulate the actions of utilities operating within their borders with respect to reliability standards for transmission and distribution delivery of electric power to retail customers in their state.

Fifty sets of different state reliability standards could undermine the reliability of the *interstate* electricity transmission system. The national standards that the NAERO process envisions will reflect state and regional input throughout the process. States should not have the authority to establish standards that affect the national standards for transmission reliability necessary to create an effective and properly functioning interstate transmission grid. If states are allowed to create standards that negatively affect national transmission reliability, it could undermine the goals of promoting electric competition in interstate commerce.

Question 9. You assert H.R. 2944 prohibits FERC merger hearings. H.R. 2944 does not eliminate hearings and maintains the discretion of FERC to hold hearings when it believes doing so is necessary to build a record to base a decision on. Do you believe FERC has to hold hearings under current law? How many of the 30 recent mergers were set for hearings?

Response. I attempted to be very precise in my testimony. I did not state that H.R. 2944 prohibits FERC merger proceedings. I did state that "H.R. 2944 would eliminate the option of *exidentiary hearings*." [emphasis added] Section 203 of the Federal Power Act provides for "notice and opportunity for hearing." H.R. 2944 would delete this language, and substitute language providing for "notice and a 60-day opportunity for oral or written presentation of views . . ." There is a significant difference between an opportunity for a hearing, which may include everything from no hearing, to a paper hearing, to a full-blown evidentiary hearing, on one hand, and the much more limited opportunity for oral or written presentation of views on the other. In our view, the opportunity for oral and written presentations provided in H.R. 2944 does not encompass evidentiary hearings. For the reasons set forth in our testimony, we do not believe FERC should be prohibited from requiring such hearings. We are concerned over the potential for mergers to frustrate rather than promote competition. FERC has found this to be the case in its evaluation of certain merger proposals.

While every merger takes at least one competitor out of the market, some mergers may promote greater competition and benefit consumers. Therefore, we do not be-

lieve FERC must hold an evidentiary hearing in every merger proceeding that comes before it, but we do believe it must have the opportunity to do so.

According to research done by FERC Commissioner Massey and presented at a recent Commission meeting, of the 30 merger applications received since the FERC adopted its new and streamlining procedures, five were received within the last five months and have not yet been processed. Of the remaining 25 cases, only three were directed to be set for hearing. These three were: American Electric Power and Central and Southwest; Western Resources and Kansas City Power & Light; and Allegheny-Duquesne. In the latter case, the applicants were offered the option of going to hearing or accepting a set of conditions to address and mitigate market power concerns. That merger was subsequently placed on hold (in our view, for reasons unrelated to FERC's action). Thus, only two of the last 30 major merger applications have been to full evidentiary hearings. Examples of expeditious consideration include Scottish Power, which received FERC approval to acquire PacifiCorp within 98 days of its filing at FERC, and the MidAmerican Energy and CalEnergy merger; which was approved in 93 days.

FERC has a self-imposed 150-day deadline for processing merger applications. Clearly, many merger applications can be handled within that time, but some clearly cannot. The Federal Power Act directs FERC to review mergers and only approve those that are consistent with the public interest. It is simply, not possible, and in our view not appropriate, to ask FERC to examine extremely complex transactions and determine whether they are indeed consistent with the public interest, and to do so within time constraints legislated by Congress.

RESPONSES OF DAVID NEVIUS, VICE PRESIDENT OF THE NORTH AMERICAN ELECTRIC RELIABILITY COUNCIL TO QUESTIONS FROM HON. JOE BARTON

Question No. 1: Is there a way to provide for enforceable reliability standards without providing for some additional Federal authority to enforce standards? Can private organizations such as NERC assume police powers or compel transmission owners or bulk power users to join NERC? Can there be enforceable reliability standards without a Federal role?

Answer: No, I don't believe it is possible to have enforceable reliability standards without some additional Federal enforcement authority, for three reasons. First, the Federal Energy Regulatory Commission has jurisdiction over the wholesale sale of electricity in interstate commerce and the transmission of electricity in interstate commerce. FERC does not have clear jurisdiction over issues dealing with reliability. Following the Northeast blackout in 1965, legislation was introduced in Congress that would have given the Federal Power Commission (FERC's predecessor) clear authority and responsibility over reliability matters. But Congress never adopted that legislation. Instead, the industry formed what would become the North American Electric Reliability Council to coordinate industry standard setting on a voluntary basis, with compliance based on "peer pressure." There were no enforceable reliability standards, but that approach has served North America well for more than three decades. It is the emergence of competition in the electric industry that now calls that approach into question.

Second, FERC does not have jurisdiction over all entities that must interact to maintain the reliability of the interstate, international high voltage electric transmission system. FERC does not have jurisdiction over the utilities within the Electric Reliability Council of Texas, the Tennessee Valley Authority, the Federal power marketing administrations (Bonneville Power Administration, Southeastern Power Administration, Southwestern Power Administration, and Western Area Power Administration), the municipally- and state-owned utilities, and the rural electric cooperatives that have financing from the Rural Utilities Service. Those entities account for approximately 30 percent of the transmission assets in this country.

Third, policing and enforcement is inherently a governmental function. Absent governmental authorization, such as exists in the securities laws for the stock exchanges and National Association of Securities Dealers to operate under Securities and Exchange Commission oversight, NERC cannot assume police powers nor can it compel transmission providers or bulk power system users to become members.

For these reasons, NERC proposes creation of an independent industry self-regulatory reliability organization under FERC oversight. This plan follows the self-regulatory models of the securities industry. The new organization would have the authority to set and enforce mandatory reliability standards. This approach capitalizes on the electric industry's technical expertise in this highly complex area, while also providing the governmental presence needed to assure the fairness and validity of the enforcement process.

Question No. 2: There are some differences between the proposed NERC reliability language and the reliability provisions of H.R. 1828. Please provide comments on those differences, and indicate whether you believe H.R. 1828 is an improvement over the NERC proposal.

Answer: The reliability provisions of H.R. 1828 are essentially the same as the NERC reliability language, with three significant exceptions. (Section 601(a) of H.R. 1828 would add a new section 218, dealing with reliability, to the Federal Power Act; the section references below are to that new section 218.)

The first important difference deals with governance of the new industry self-regulatory organization. The NERC language provides for governance by a "board wholly comprised of independent directors." H.R. 1828 (section 218(e)(4)(E)) changes that to governance by a "board of no more than eleven members, one of whom shall be appointed by the Secretary of Energy." That change is unacceptable to NERC and the coalition that is supporting the NERC language. The fundamental premise of the NERC reliability legislation is to have an *industry* self-regulatory organization operating under government oversight. Permitting the Secretary of Energy to designate a representative on the board would put the government into the organization itself More importantly, the NERC proposal calls for *independent* directors, that is, directors who do not have an interest in other market participants. This independence requirement is omitted in H.R. 1828. This omission has consequences even beyond the Department of Energy and could transform the board for the new reliability organization from an independent one to a "stakeholder" board—a significant change. The Federal power marketing administrations, for example, are part of the Department of Energy. The Secretary of Energy, therefore, is not "independent" from other market participants, but is a stakeholder in the industry. Finally, the high voltage transmission system is *international* in nature. The proposed new reliability organization provides a means for interests from the U.S., Canada, and, as appropriate, Mexico, to participate together in reliability standards development and enforcement. The provision of H.R. 1828 that would place a representative of the United States government in the governing structure of the new reliability organization has already raised significant questions from Canadian participants.

The second significant difference between the NERC language and H.R. 1828 concerns the treatment accorded Federal power marketing administrations, the Tennessee Valley Authority, the Bureau of Reclamation, and the Corps of Engineers, as well as requirements of the Nuclear Regulatory Commission. Section 218(k) of H.R. 1828 states:

> "Any actions taken under this section by the Commission, the Electric Reliability Organization, and any Affiliated Regional Reliability Entity shall be consistent with any statutory or treaty obligation of a Federal Power Marketing Administration, the Tennessee Valley Authority, the Bureau of Reclamation and the Corps of Engineers and any Nuclear Regulatory Commission requirements."

There is no comparable provision in the NERC language, and NERC sees no basis for including such a provision. The provision appears to establish an additional substantive standard that any actions by the self-regulatory organization must meet for these identified electric market participants. NERC knows of no reason why these entities should be given special status when it comes to reliability, or why these entities should not be bound by the same reliability rules that would bind all other participants in the electricity markets. The Commission, the Electric Reliability Organization, or an Affiliated Regional Reliability Organization cannot change a statutory or treaty obligation of these entities, any more than they can change any other law to which other electric industry participants may be subject, including, for example, clean air laws. NERC therefore recommends that this provision not be included in any reliability legislation that moves forward.

The third significant difference between the NERC language and H.R. 1828 concerns the application of the antitrust laws. Under the NERC language, activities of the Electric Reliability Organization and its Affiliated Regional Reliability Entities, as well as the activities undertaken in good faith under the rules of those organizations by members of those organizations, are rebuttably presumed to be in compliance with the antitrust laws. Under the provisions of H.R. 1828 (section 218(o)), the conduct of the Electric Reliability Organization, its Affiliated Regional Reliability Entities, and members of those organizations, to the extent that conduct is undertaken to develop or implement an Organization Standard that is approved by the Commission under other provisions of the legislation, would not be deemed illegal per se. Such conduct would be judged on the basis of its reasonableness, taking account all relevant factors affecting competition.

NERC believes that the antitrust provisions of H.R. 1828 are too restrictive. More than in any other industry, the cooperative actions of participants in the electric industry are crucial to being able to maintain the reliable operation of the trans-

mission grid. Market participants should not have disincentives to engaging in the necessary cooperative behavior. By establishing the presumption, although rebuttable, that the actions of the reliability organization and its regional affiliates are legal, NERC's approach offers the needed assurance to industry participants that engaging in the cooperative actions necessary to maintain a reliable bulk power system will not subject them to antitrust liability. The presumption of antitrust law legality is justified by the oversight authority given to FERC over the reliability organization's governance procedures and development and enforcement of standards.

NERC therefore recommends that the original antitrust provisions of the NERC language be substituted for those in section 218(o) of H.R. 1828. If this cannot be accomplished, several technical issues in this H.R. 1828 language should at least be addressed. These include:

1. Omission of "enforcement" from protected activities. The H.R. 1828 language states that conduct undertaken to "develop or implement" standards is not deemed illegal per se, but it makes no mention of "enforcement." The responsibilities of the Electric Reliability Organization and its affiliates and members are to "develop, implement, and enforce" reliability standards. "Enforcement" should be included as a protected activity.
2. Focusing the "reasonableness" language exclusively on effects on competition. H.R. 1828 specifies that conduct is to be "judged on its reasonableness, taking into account all relevant factors *affecting competition* (emphasis added)." Some of the activities of the Electric Reliability Organization, its affiliates and members in setting and enforcing standards for the reliable operation of the grid will likely have the effect of restricting competition, because that is necessary in order to maintain reliability. Having such activity judged based only on matters affecting competition eliminates half the equation. While we recommend retention of the original NERC language, if any 66 reasonableness" standard is to be included, NERC strongly recommends that the language be revised to include impacts both on competition and reliability. Alternatively, the standard could be one of "reasonableness, taking account of all relevant factors," without highlighting any particular factor.
3. Limitation of antitrust protection to actions "approved by the Commission under subsection (O)." NERC recommends that this clause be deleted. Otherwise, this language raises at least two significant issues. First, what are the implications of this language for standards that are adopted and enforced on an emergency basis prior to "approval" by FERC? Second, is any antitrust protection available under the language of H.R. 1828 for an existing Organization Standard that is suspended under subsection (0(3)(b)?

In addition to these three significant differences, H.R. 1828 provides for an Electricity Outage Investigation Board within the Department of Energy (section 602 of H.R. 1828). This additional governmental agency is unnecessary. Both the NERC language and H.R. 1828 would establish the Electric Reliability Organization as an independent, industry self-regulatory organization, with FERC overseeing that organization. An Electricity Outage Investigation Board within DOE would simply duplicate the efforts of the new reliability organization and FERC.

The remainder of the differences between the NERC language and the reliability provisions of H.R. 1828 are of either a clarifying or conforming nature. NERC has no objection to those other changes.

Question No. 3: There are concerns about how transmission constraints impede interstate electric sales. Where are the major constraints—which States and regions have the worst constraints? How do these transmission constraints limit interstate commerce in electricity?

Answer: Transmission constraints limit interstate commerce in electricity because they restrict the amount of power that can be moved from one part of the country to another at a particular time. The constraints arise from the physical configuration of the generation and transmission facilities. The constraints can be one of three different kinds—thermal limits, voltage limits, or stability limits.

- Thermal Limits: Thermal limits establish the maximum amount of electrical current that a transmission line or electric facility can conduct over a specified time period before it sustains permanent damage by overheating or before it violates public safety requirements. System operators must constantly monitor actual flows throughout the network to ensure that the power flows do not exceed these limits. Operators must also monitor for "contingency" limits, that is, to ensure that the power flow on any one facility will not exceed its limit following the sudden loss (outage) of any other facility. (Since electrical power flows readjust instantaneously, the system must at all times be operated in this preventive mode.)

- Voltage Limits: System voltages and changes in voltages must be maintained within a range of minimum and maximum limits. Voltage limits establish the maximum amount of electric power that can be transferred without causing damage to the electric system or customer facilities. A widespread collapse of system voltage can result in a collapse of portions or all of the interconnected network.
- Stability Limits: The transmission network must be capable of surviving disturbances (e.g., generators tripping off, lightening strikes, wind damage to conductors) through the transient and dynamic time periods (ranging from milliseconds to several minutes) following a disturbance. All generators connected to ac interconnected transmission systems operate in synchronism with each other at the same frequency (nominally 60 Hertz). Immediately following a system disturbance, generators begin to oscillate relative to each other, causing fluctuations in system frequency, line loadings, and system voltages. For the system to be stable, the oscillations must diminish as the electric systems attain a new, stable operating point. If a new, stable operating point is not quickly established, the generators will likely lose synchronism with one another, and all or a portion of the interconnected electric systems may become unstable. The results of generator instability may damage equipment and cause uncontrolled, widespread interruption of electric supply to customers.

NERC's Planning Standards and Operating Policies set parameters within which the system must be designed and operated in order to avoid exceeding any of these limits.

Twice a year, NERC reports on its assessment of the reliability of the electric system for the upcoming season, examining both generation adequacy and transmission adequacy. While the location of transmission constraints can vary from time to time, depending upon how the system is configured, what load is being served, and what generators are online, the NERC reliability assessments give a general picture of where transmission constraints are likely to occur. I have attached a copy of *NERC's 1999 Summer Assessment* (released June 1999) to my answers. The summaries of the Regional assessments, beginning at page 21 of the Summer Assessment, give a general indication of where transmission constraints can be expected under base case conditions, However, as conditions depart from the base case either because of equipment outages or higher-than-expected demand, transmission constraints may be more severe or arise in other areas than indicated in the report. As stated in the Executive Summary of the 1999 Summer Assessment, "[i]mprovements to the transmission system are not keeping pace with the demands being placed on the system."

Question No. 4: What is your position on the FERC proposed rules on RTOs? In particular, do you think the pricing provisions will encourage expansion of transmission and remove constraints?

Answer: NERC told FERC in comments filed August 23, 1999, that properly functioning RTOs could help the industry deal with the challenges it faces, but that RTOs were not the whole answer. NERC identified four challenges facing the electric industry: the current balkanization of the transmission grid; the mismatch between how business is arranged and how power actually flows; transmission pricing and compensation issues, and the huge increase in the number and complexity of transactions. With regard to transmission pricing, NERC said the following:

> "Transmission rates must provide incentives to get the right amount of transmission infrastructure built. The cost of transmission is a relatively small part of the overall price of delivered power. We must make sure that shortages of transmission capacity do not restrict power flows and limit the benefits that otherwise could be achieved from competitive electricity markets."

In the notice of proposed rulemaking, FERC expressed a willingness to be flexible about transmission rates and to entertain incentive rates as an inducement to get companies to join an RTO. The Commission did not directly take on the linkage between transmission rate reform and needed expansion of the transmission system. NERC believes that this is a subject that the Commission will need to take on directly. I have attached a copy of NERC's comments to these answers.

Question No. 5: H.R. 1828 and H.R. 2050 authorize compacts to plan and site transmission lines. Do you think States will delegate their siting authority to such regional bodies?

Answer: NERC thinks it unlikely that states will delegate their siting authority to regional bodies in a way that effectively deals with siting new transmission, although regional planning efforts may be productive. In certain parts of the country (New England, for example) there is considerable experience in states working together to address regional problems. But the problems facing the industry today are often siting new lines between what have been traditional regions. NERC's Annual

Ten-Year Reliability Assessments cite a number of examples of these difficulties. I have attached a copy of NERC's Ten-Year Reliability Assessment for the period 1998-2007 to these answers. Unless the regional bodies were sufficiently large to include what are now "boundary" problems, giving a regional body siting authority may not be effective.

Moreover, siting new transmission lines has become one of the most contentious issues facing state authorities. NERC does not believe that state authorities would willingly give up control over matters that their citizens feel so strongly about.

One additional factor is increasingly present. Federal land management and resource agencies are playing a growing role, for example under the Federal Land Management Policies Act, in deciding whether and where additional transmission facilities can be built. Regional compacts would not be effective in these circumstances unless federal agencies are willing and able to turn over their own siting authorities.

RESPONSES OF GLENN ENGLISH, CEO, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION TO QUESTIONS FROM HON. JOE BARTON

Question 1. You propose removing limits on cooperative business activity. My understanding is Federal law imposes no limits on cooperative business activity, and any limits are set by State law. Do you agree? If so, aren't you really asking Congress to preempt State cooperative laws?

Answer. The Public Utilities Holding Company Act (PUHCA) places federal barriers on the diversification activities of investor-owned-utilities. State laws tend to provide the barriers to the diversification activities of electric cooperatives. If Congress is going to remove the barriers provided by PUCHA for the largest utilities in the land, it should also remove the barriers for the electric cooperatives.

Question 2. One thing we have heard loud and clear the past four years is the need to respect the States. States have authority to remove limits on cooperative business activity. If States have the authority and the willingness to address this issue, why should Congress preempt them?

Answer. State laws limiting electric cooperative business activity were created for an earlier time. If there is to be no changes to federal laws governing the electric industry, there is no need to change state laws limiting electric cooperative business activity. However, if competition is to be the result of changed federal laws, then it makes no sense to allow barriers to continue to exist to prevent members of electric cooperatives from providing themselves with the diversified services they want through their cooperative. Cooperatives are an important segment of the electric industry, and thus, an important constituency for the Commerce Committee. To make competition truly vigorous, people will need the authority to provide the level of service they want for themselves through an electric cooperative.

Question 3. Do you believe only cooperatives should qualify for an exemption from FERC transmission regulation or should municipal utilities or IOUs with small transmission systems also be eligible for an exemption?

Answer. Electric cooperatives are consumer-owned. If you take service from an electric cooperative, you are a member-owner of that cooperative, and have a voice in the operation of it. That is completely different from investor-owned-utilities that are operated to make a profit from customers for the benefit of absentee stockholders. The difference is truly significant for the concept of regulation. Courts and Public Service Commissions across the nation have repeatedly held that consumers can operate their own consumer-owned systems according to their own needs without the necessity of being protected by an agency of the Government. Local ownership, local control and local autonomy are a more powerful force for consumer protection than absentee regulators.

Additionally, true, effective competition for retail electric service cannot be imposed by a remote, heavy handed, federal bureaucracy attempting to force every supplier to be the same as every other supplier. Retail competition will come from differences among participants, and from the ability of participants to be different and to offer different and new ideas, and from the ability of participants to appeal to different market niches and to address unique local circumstances. Size is definitely a significant consideration; other issues are the extent of integration of the transmission facilities with the bulk power system and the ownership structure.

Question 4. You propose exempting cooperatives from FERC merger review because cooperatives are so small that mergers are unlikely to raise market power issues. Should mergers involving other small electric utilities also be exempt from FERC review?

Answer. Electric cooperatives should be exempt from FERC merger review in part because they are small; in part because they are consumer-owned, and in part because they are subject to merger review at the Rural Utilities Service (RUS), a federal agency within the U.S. Department of Agriculture, as a consequence of loan funds for the construction of electric facilities in rural areas. As the mortgage holder, RUS has the ability to prevent a merger, or suggest alterations to merger terms. Subjecting electric cooperatives to merger review by two federal agencies with dissimilar agendas is a prescription for trouble.

As regards FERC's responsibility for protecting against market power, NRECA and the American Public Power Association (APPA) jointly filed a petition at FERC suggesting a moratorium on investor-owned-utility mergers in excess of 1,000,000 customers until Congress completes its work in creating a competitive environment for retail electric sales. FERC did not act on the petition. Small system mergers are of much less risk to the market than large system mergers and should be subject to different standards of review.

If two consumer-owned systems want to merge, why should FERC be involved? Consumers do not need FERC to protect them from themselves in a merger case.

Question 5. RUS does review cooperative mergers, but my understanding is they do so from the point of view of a banker and are only concerned about loan recovery. Does RUS consider market power issues when they review cooperative mergers?

Answer. The principle focus of RUS in a merger case seems to be the repayment of the loan, the value of the mortgage and, furthering the objectives of the rural electric Act, which is intended to insure affordable, reliable electricity to consumers. Moreover, additional federal review of cooperative mergers, focused on market power, is unnecessary in part because cooperatives are so small. RUS is the mortgage holder on about $32 billion in loans to electric cooperatives to provide facilities to serve people in rural areas. The American Electric Power Company (AEP) sold more electric power last year than all the electric cooperatives in the nation combined. The repayment of the RUS loan and the value of the mortgage is affected by market power in that electric cooperatives do not have market power in the sense that they can dominate a market.

Question 6. You express concern about the States setting individual transmission reliability standards. Would 50 different transmission reliability standards improve reliability? Would 50 different standards burden interstate commerce?

Answer. Fifty different bulk transmission system reliability standards would not accommodate reliability or interstate commerce. NRECA supports a continued state role in preserving reliability of the local distribution systems

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RESPONSES OF LYNNE H. CHURCH, EXECUTIVE DIRECTOR, ELECTRIC POWER SUPPLY ASSOCIATION TO QUESTIONS FROM HON. JOE BARTON

Question 1. You propose granting FERC jurisdiction over transmission used to make bundled retail sales. What is the position of the States on this issue?

Response. We presume that the states' position on this issue will vary from state to state, with some opposing and some supporting. In 24 states, for example, retail competition in electricity markets has already been embraced. A key element of this process is the decision to "unbundle" the components of electricity transactions and separate the costs of generation from those associated with transmission and distribution services. For these 24 states, therefore, there will be *no direct long-term impact* from the change in legislative policy that we propose.

The lack of direct impact, however, does not imply that these 24 states or the remaining states will be indifferent to this issue. In many states, the cost of power to consumers will be increasingly and directly linked to access to a viable, robust wholesale power market. A state that relies on an interstate wholesale market has to be vitally concerned about the codification of rights for other states to place the equivalent of toll booths on the interstate electricity grid. Thus, *any* state that has come to rely on competitive wholesale markets should be very concerned by the bill's clear split in regulatory authority over the interstate grid.

Experience has shown that even small disruptions or curtailments of transmission at distant locations can result in dramatic price impacts. During the hearing process, one Subcommittee member stated that he trusted his own state's public utility commission more than he trusted FERC. *This is not a correct reflection of the issue at hand.* The proper question is whether a policymaker trusts *another* state's public service commission more than the FERC.

Many states, we believe, are coming to recognize the value of a single regulatory body to have oversight responsibility and set consistent "rules-of-the-road" for the interstate grid. At an earlier Subcommittee hearing, representatives from Ohio and

Pennsylvania said as much in response to members' questions. What these states are realizing is that; without consistency, there will be no investor confidence; without confidence, there will be no robust, competitive wholesale power market; and without a robust, competitive wholesale market, many of the consumer benefits promised during the state's debate over retail restructuring will not appear.

Question 2. You say H.R. 2944 interjects States into FERC determinations of transmission and distribution facilities, by providing deference to State views. Don't States already have a role in such determinations? FERC granted them a role 3 years ago in Order 888, but providing for deference to State views.

Response. EPSA believes absolutely that the States have a role to play in these determinations. However, *whether* the states have a role is not the critical issue for EPSA members. Our concerns center on the extent of this involvement and, most critically, whether local interests and issues will be allowed through a legal guarantee of "deference" to trump the general, national interest. As a simple way to address these concerns we have suggested that the legislation be amended to include the phrase "provided such action is not contrary to the public interest" at the end of Section 101 (e).

It is true that FERC agreed to grant deference to the states on these issues in Order 888. However, we believe that there is an enormous qualitative difference between a decision made by an independent regulatory body to grant deference to an entity and a requirement of deference included in public law. In general, EPSA would express concern or opposition to the specific language of Orders 888 and 889, were the Subcommittee to choose to codify the decisions embodied in those orders as law. These orders are complex and the public context is evolving. In the gas industry, for example, the Commission's Special Marketing Programs led to Orders 436 and 451, which led in turn to Order 636. Law, on the other hand, is often relatively static and inflexible. EPSA is concerned that legislating deference to the states, as drafted, will create a legal straightjacket for FERC and obstruct the public interest.

Question 3. You oppose FERC deference to the States in determination of transmission and distribution facilities, which is the approach FERC laid out in Order 888. Is FERC giving too much deference to the States. Can you give examples? You indicate utilities are trying to reclassify facilities. Is FERC agreeing to this reclassification?

Response. As stated above, EPSA does not oppose some deference by the FERC to state commissions. The question centers on the degree of deference and whether local issues are allowed to trump the national interest.

It is impossible today to answer the question as to whether FERC is giving "too much" deference to the states. The issue of "refunctionalizing" transmission assets is a relatively new one and is currently before the Commission in at least one case. Until FERC acts, we cannot say.

However, we strongly believe that this is a very significant issue and threat to the interstate grid. As competition takes hold, utilities may attempt to shift assets between state and federal jurisdiction as one way to exercise market power.

Evidence is mounting that transmitting utilities have already begun to abuse FERC's "seven part test." The American Public Power Association recently released a report by Whitfield Russell Associates with some troubling statistical information on this new trend. According to the report, commonwealth Edison of Chicago recently refunctionalized 40% of its net transmission plant, almost all of it to distribution, including some 345 kV facilities. Sierra Pacific Power has refunctionalized 50% of its transmission system, while Wisconsin Public Service Corporation (WPS) recently filed with the state public service commission to classify virtually all of its transmission assets as distribution. If accepted by the Wisconsin Public Service Commission, only 124 pole miles of facilities, out of 1,474 pole miles reported on WPS's 1998 FERC Form 1, will remain subject to the Commission's open access tariff.

FERC may or may not agree with these efforts to refunctonalize transmission assets. However, regardless of the specific decisions ultimately made, it makes little sense to codify an unqualified policy of deference to state decisions. If such language were in the Federal Power Act today, we would have no doubt that its effect would be to tilt the decision making process further away from the pursuit of positive, national policy.

Question 4. You say "States acting on their own" can't address generation market power? Did the New England States reduce generation market power? Did Texas reduce generation market power?

Response. Many states have attempted to address market power issues. Some plans have been more effective than others. In New England and in California, state action has resulted in the divestiture of significant electric power generation capac-

ity, which has broadened the ownership base of the existing asset base and reduced vertical integration in local power markets. In Texas, there was an attempt to reduce the concentration of ownership of generation assets, but the effort may fail. While the intention was to limit generation ownership to no more than 20% of the market, loopholes included in the legislation seem to permit at least one utility to continue to own almost 40% of the current installed capacity in ERCOT with little likelihood that significant divestiture will occur.

Notwithstanding the success (or lack thereof) of state attempts to mitigate market power, there were always be a need for a multi-state or national authority. Without question, the electricity grid is interstate. For the foreseeable future, the grid will be composed of regulated monopoly companies, many of which are and will continue to be vertically integrated with generation capacity. Actions taken in one state can directly affect the price paid for power in another state. For example, the dramatic price spikes in the Midwest wholesale market this past summer were linked to a curtailment of transmission capacity along the U.S.-Canadian border.

Given the rapidly evolving nature of the electric power industry, it is impossible to predict where and how market power will be exercised. However, as long as the grid and wholesale markets are interstate, it will be impossible for any state to fully protect its customers from anti-competitive out-of-state activity. In fact, a state may find itself unable even to identify or document the use of market power from events beyond its boundaries, much less counter or remedy it. As a result, we have endorsed the Administration's legislative language as an appropriate, minimalist legislative solution to the general issue of market power.

Question 5. You testify EPSA members do not see the courts or antitrust laws as a viable approach to resolving market power issues. What do you mean? Are you saying the market power problems you are worried about don't rise to the level of antitrust law violations or it takes too long to bring an antitrust action?

Response. Antitrust laws represent a powerful tool to address market power. However, this tool, in general, is extraordinarily expensive to apply and, when used, slow to achieve results. For example, the electricity trade press reported last summer about a court decision supporting a group of municipal utilities in an antitrust action against an investor-owned utility on an allegation of discriminatory access to the grid. When you read the article, you discover that (1) the order to open the utility's system originated in 1980, (2) the discriminatory activity occurred in 1989, (3) an earlier court agreed with the municipalities in 1993, and (4) notwithstanding the latest court action, the investor-owned utility is still denying that the recent decision is final.

Subcommittee members need to understand that the electric power industry is rapidly and dramatically changing. Companies are entering and exiting the industry on an almost daily basis. These companies cannot rely a process that takes a decade or more for justice to unfold.

In addition, we do not expect that every instance where the issue of market power raised to require a court suit for resolution. In some instances, the issues may be minor and need only a modest regulatory intervention to address. Some anti-competitive activities may be, frankly, inadvertent and more a result of mindset ("this is the way we've always done it") than a conscious decision to advantage the monopoly provider. Without flexibility in policy and the ability to resolve these issues in near "real-time," the advantage of those with potential market power will only increase. If one company understands that its competitor lacks the financial wherewithal to survive a lengthy legal battle, a clear advantage lies with the stronger company.

RESPONSES OF JACK BRICE, MEMBER, BOARD OF DIRECTORS, AARP TO QUESTIONS OF HON. JOE BARTON

Question 1. Some propose deleting the consumer protection provisions from H.R. 2944, arguing State have authority to address these issues. Should consumer protection provisions be included in Federal legislation?

Response. Unquestionably, consumer protection provisions should remain in Federal legislation. In testimony before your Subcommittee, AARP stressed the importance of consumer protection provisions in federal electric utility restructuring legislation. We view the Title III provisions in H.R. 2944 that address "slamming," "cramming," information disclosure and privacy as a necessary consumer protection floor. Absent federal guidelines, consumers could be subjected to the types of deceptive and misleading practices that have plagued the telecommunications industry. Further, we hope that states will act independently to strengthen the provisions you have introduced in the federal bill.

AARP is not alone in its support of federal consumer protection provisions. Both federal and state-based consumer advocacy groups have publicly stated the need for a federal role in this area. For example, at the October 5 & 6 hearings on H.R. 2944, the National Association of State Utility Consumer Advocates (NASSUCA), the Consumer Federation of America (CFA) and the Regulatory Assistance Project (RAP) all testified in support of Title III.

AARP believes that for competition in the electric utility industry to work, strong federal consumer protection laws must be applied to the sale and service of electricity in a restructured environment to prevent abuse in the marketplace. Title III of H.R. 2944 supports that belief and should be retained in any subsequent versions of the bill.

Question 2. You support municipal opt outs, or forced aggregation, such as proposed by Mr. Brown. Why should municipalities have a preference in aggregation?

Response. AARP supports the residential opt-out aggregation concept in Mr. Brown's (D-OH) legislation, H.R. 2734. We do not however, embrace the exclusivity givens to municipalities in the bill. In actuality, AARP prefers the language currently in H.R. 2944. In discussions with Members of the Subcommittee and staff over the past two months, we have been promoting a more expansive definition of aggregation than the one proposed by Mr. Brown. We believe that Title V of H.R. 2944 achieves that goal by allowing "any entity that aggregates consumers" to acquire retail electric energy on an aggregate basis.

However, as we testified on October 6, we would like to see opt-out aggregation facilitated rather than an opt-in plan. Opt-out aggregation would ensure that a majority of underserved consumers could reap the benefits of lower rates. Both opt-out aggregation and expanding the number of groups eligible to aggregate are consistent with AARP's overall goal of ensuring that residential customers benefit from competition in the electric utility industry.

Question 3. You say that H.R. 2944 places the "full burden" of universal service programs on the States. Isn't that where the burden is now? Outside of programs like LIHEAP and weatherization, isn't universal service a State responsibility?

Response. You are correct, Mr. Barton. Currently, the burden of maintaining universal service programs is fully on the shoulders of the states. While not necessarily ideal, ensuring electric service to all has been manageable in large part due to the monopolistic nature of the industry. AARP is concerned that a competitive marketplace will displace the existing "obligation to serve," putting more pressure on the states to monitor the delivery of power to all residents.

Federal programs like LIHEAP and weatherization do provide some needed assistance in today's utility environment. However, the annual battles over adequate appropriations for these necessary programs leaves doubt that the programs can continue to exist in their current forms. More certainty is needed. AARP supports a universal service program, administered by a Joint Federal-State Board and funded by a per kilowatt hour charge that is assessed to all providers of electricity. We strongly suggest that this assessment come from general revenues and not become a line-item on consumers monthly billing statements.

TRUTH-IN-BILLING REQUIREMENT

This section is in response to your question to Jack Brice at the October 6 hearing. You inquired as to what AARP meant by "truth-in-billing" as neither you nor Mr. Hall "could be opposed to 'truth-in-billing.'"

As AARP has testified to previously, we envision that a "Truth-in-Billing" requirement will make it easier for consumers to read their monthly billing statements, recognize who is providing service, what they are paying for it and who they can call if they have questions. We believe that such a provision will reduce the incidences of "slamming" and "cramming" and that it will complement the information disclosure provisions of H.R. 2944 nicely.

RESPONSES OF RAJ RAO, INDIANA MUNICIPAL POWER AGENCY TO QUESTIONS OF HON. JOE BARTON

Question 1. You propose "complete separation of transmission control from generation interests." Do you propose mandatory divestiture of transmission?

Response. TAPS does not propose mandatory divestiture of transmission. Rather, TAPS proposes that FERC be given the authority to require transfer of the *control* of transmission facilities (along with sufficient control over generation to permit reliable operation of such transmission facilities) to an RTO with broad regional scope. TAPS proposes that FERC be empowered to require divestiture of transmission only if it finds it necessary to achieve truly independent RTOs.

The complete separation of transmission from generation interests discussed in TAPS' testimony refers to the critical RTO characteristic of independence, not particular corporate forms. We feel strongly that the RTO must be structured so that no transmission owners (or other market participants) can control or influence the RTO. Thus, we oppose the provisions in H.R. 2944 that permit market participants to retain up to 10% of voting interests and unlimited "passive" interests (which include a voice in certain decisions) as severely undermining the fundamental concept of an independent regional grid.

TAPS has not taken a position on the transco vs. ISO debate. Both structures can work *if* they are truly independent, have the appropriate and broad geographic scope, and have authority to operate, plan and expand the transmission system.

Question 2. You propose granting RTOs authority to require construction. Do you propose giving RTOs authority to site transmission lines?

Response. While TAPS would not object to giving RTOs authority to site transmission lines, RTO siting authority is not a part TAPS' RTO proposal, nor is it necessary to the TAPS proposal. Rather, what is critical is that the RTOs have the authority to identify the transmission upgrades necessary to meet the needs of all users and for system reliability, and to require implementation of those upgrades by the existing transmission owners or others, *e.g.,* by bidding out construction to third parties (a non-regulatory, market-based solution to ensuring construction of needed transmission). The RTO or the entity responsible for construction would need to obtain whatever siting approvals are required. TAPS assumes that the RTOs finding that an addition was necessary to meet regional needs would assist in the siting process.

I note that while TAPS does not now have a position on siting authority, I personally believe that federal siting authority could assist in assuring that the transmission needed to support competitive interstate power markets is constructed.

Question 3. You propose granting FERC jurisdiction over transmission used to make bundled retail sales. What is the position of the States on this issue?

Response. TAPS believes that it is essential to the bill's intent of facilitating retail competition that FERC be clearly given authority over all transmission service, whether bundled or unbundled. As explained in our testimony, competition cannot develop on a state by state basis if one state has the authority to grant a higher priority to "bundled" power deliveries to its citizens, while relegating unbundled transmission to out-of-staters to second class status. TAPS recognizes that some states are seeking this authority, but we believe such efforts are short-sighted. At its core, this issue is not a state vs. federal matter, but rather a state vs. state issue that demands a federal solution.

Question 4. You say H.R. 2944 allows large incumbent utilities to foreclose competition. Can utilities foreclose competition without violating antitrust law?

Response. Yes, as A. Douglas Melamed, Principal Deputy Assistant Attorney General, Antitrust Division, Department of Justice, testified before your Subcommittee on May 6, 1999 (at 6):

> Let me now turn to the issue of market power. Because of the existing structure of the electric power industry, there are likely to remain significant market power problems in the transmission and generation of electricity, even as the industry is restructured to increase the role of competitive market forces.
>
> The authority of the Department of Justice to enforce the antitrust laws with respect to the electric power industry does not sufficiently address the ability of electric utilities to exercise market power that can thwart free competition within the industry. The antitrust laws do not outlaw the mere possession of monopoly power that is the result of skill, accident or a previous regulatory regime. Antitrust remedies are thus not well-suited to address problems of market power in the electric power industry that result from existing high levels of concentration in generation or vertical integration.

For example, if one utility, by virtue of its history as a state-sanctioned monopolist, owned most of the generation within a market area, and there was limited transmission capacity to import power from alternative sources, merely declaring there to be choice would relegate consumers to purchasing their essential electricity requirements from the worst of all worlds—a deregulated monopolist that would be free to increase price above the level that would result from effective competition. Foreclosure of competitors would result from past regulatory regimens and past decisions about the siting and construction of generation and transmission that created the current topography of the transmission grid, not necessarily a violation of the antitrust laws.

Indeed, market power can be conferred by ownership of strategically-located generating units which, because of the configuration of the transmission system and the location of generation in a given area, "must run" for reliability purposes (*e.g.,* to

maintain voltage levels under particular conditions). Without violating the antitrust laws, the owner of such "must run" units is in a position to take advantage of its market power by "naming its price" (acting as a monopolistic "pricing maker," instead of a competitive "price taker") during time periods when the unit "must run" units even in otherwise deregulated generation markets.

Question 5. You testify that "individual states will be powerless to effectively address this problem." Did California reduce generation market power? Did the New England States reduce generation market power? Did Texas reduce generation market power?

Response. Mere divestiture of one utility's generation, in bulk, to a different owner in an effort to quantify and reduce stranded costs does not reduce generation market power. While the presence of the California ISO and ISO-New England have the effect of reducing market power, significant generation market power remains. Indeed, reports submitted to or by the new institutions illustrate that neither California nor the New England States, acting individually or in concert, have eliminated the generation market power that threatens to deprive consumers of the benefits of competition.

For example, the March 9, 1999 "Second Report on Market Issues in the California Power Exchange Energy Markets," prepared by the Market Monitoring Committee of the California Power Exchange, and filed at FERC in *AES Redondo Beach, L.L.C., et al.,* Docket Nos. ER98-2843, *et al.,* reports continuing exercise of market power. *See,* for example, the report's description of bidding behavior (at 57, emphasis in original):

> [M]any of the generators sometimes bid as if they have market power, rather than as price-taking competitors. To put this another way, not only did the generators *have* the ability to affect the market price at times, but they also *acted* to exercise that market power

The report also states (at 64) that "at various times most of the new owners of generation divested by the California investor-owned utilities "held back substantial amounts of capacity from the PX Day-Ahead market. The amount offered (at any price) in the PX market was often much less than the firm's effective capacity." While the authors of the report did not have enough information to identify precisely why capacity was withheld, the report observes (at 64): "To the extent that there was withholding of capacity from the PX market, whether to meet anticipated ISO demands or deliberately to raise prices, it would have the effect of further raising prices in the PX market." The report concluded (at 66-67) that "during some hours there was considerable potential for generators to exercise market power in the PX market . . . At these and other times, some [generation owners] bid in a way that is consistent with an attempt to exercise market power, and prices were high at these times." The report warned (at 68) that forces "if not countered, may lead to more frequent and more severe episodes of high prices in the future." Significantly, as reported in the oral testimony before the Subcommittee of Marty Kanner on behalf of the Consumers for Fair Competition, investor-owned utilities in California have sought FERC assistance in restraining the exercise of market power in California.

Similarly, notwithstanding deregulated generation markets, ISO-New England had to invoke Market Rule 15 (imposing temporary price caps) more than 100 times this past summer to correct market deficiencies. At the request of ISO-New England, FERC recently approved ISO-NE authority to impose interim price caps to correct market flaws during periods of capacity shortage, noting (at 4): "Generators, it appears, are bidding strategically to set the market clearing price during [capacity shortage] conditions. At these times, all bids must be selected so there is no effective price limit on the bids."[1] *ISO New England, Inc.,* FERC docket No. ER99-4002-000, issued September 30, 1999. Significantly, the New England Conference of Public Utilities Commissioners submitted comments on September 22, 1999 supporting the interim caps, explaining (at 1-2): "NECPUC has worked hard to ensure that ISO New England has the authority and tools necessary to monitor the electricity markets for design flaws, competitiveness and efficiency."

The recognition by the New England States that they cannot alone "solve" continuing and significant generation market power problems is further highlighted by NECPUC's August 23, 1999 comments to FEC in the RTO rulemaking proceeding, FERC Docket No. RM99-2-000 (at 17-18, emphasis added, footnote omitted):

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[1] The portion of the underlying report that describes "bidding behavior" has been withheld from the public at this time on grounds of confidentiality. *See* Review of Reserves and Operable Capability Markets: "New England's Experience in the First Four Months, Preliminary Draft dated October 1, 1999, by Peter Cramton, Professor of Economics, University of Maryland and President of Market Design Inc.

> Th[e market monitoring] function should be expanded to include mitigation of market flaws and power, and not be limited merely to monitoring the markets. The Commission proposes that the RTO be required to monitor markets for transmission services, ancillary services and bulk power to identify design flaws add *market power* and propose appropriate remedial actions . . .
>
> We agree that it is essential for an RTO to monitor the markets. However, to be effective, RTOs must have unequivocal authority to enforce violations of market standards and back those findings with real sanctions and penalties. Failure to have such authority will, at best permit, and at worst encourage, anti-competitive activities by market participants. Those anti-competitive activities could easily negate the efficiency and cost savings gained by opening up competitive wholesale markets.
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> Therefore, in addition to the monitoring requirements proposed by the Commission, NECPUC strongly recommends the adoption by RTOs of formalized *market power monitoring and mitigation rules* such as those available to ISO New England. Market Rule 13 authorizes ISO New England to impose sanctions when market participants, through their actions, threaten to impair short-term reliability or competitiveness of the *regional* market, and Market Rule 15 allows ISO New England to use emergency corrective actions to remedy market design and implementation flaws. Adoption of such rules by an RTO will . . . help assure that RTOs meet the Commission's goal of a competitive market.

As the NECPUC comments highlight, generation markets are regional and, with limited exceptions, are not confined to a single state. A state has limited ability to address what is necessarily a multi-state problem. Indeed, a growing number of utilities span multiple states and even multiple regions. No one state has jurisdiction to solve the problem. By analogy, assuming the big three automobile manufacturers were engaged in price fixing, you wouldn't want to deny the Department of Justice the authority to sue because a single state could do so. The same is true here.

The portion of Texas covered by the Electric Reliability Council of Texas, which is connected to the integrated North American grid only by DC ties, is one of those exceptional circumstances where the electricity market is more confided. Some of the approaches adopted in the Texas legislation, such as the provisions for divestiture and capacity auctions, could be effective tools to reduce market power. However, for those states that are part of the Eastern or Western Interconnections, state efforts to address what are inherently regional market power problems (as acknowledged by NECPUC) are likely to be far less effective than federal authority to address market power.