

# DOE's Notice of Inquiry on Mandatory Electric Reliability Standards

## Comments of Industrial Consumers

The Electricity Consumers Resource Council (ELCON) and the American Iron and Steel Institute (AISI) (together, Industrial Consumers) file these comments in response to the Department of Energy's Notice of Inquiry on Electric Reliability Issues published in the Federal Register on November 20, 2000. Industrial Consumers commend the Department of Energy (DOE) for initiating this notice of inquiry. A new Administration and a new FERC represent a new opportunity to take a fresh look at how the nation's electricity markets should be maintained.

### NOTICES AND COMMUNICATIONS

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## DESCRIPTION OF COMMENTERS

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

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

## EXECUTIVE SUMMARY

In these comments Industrial Consumers make general observations about reliability and respond specifically to the questions posed by DOE in the November 20, 2000 Notice of Inquiry. Reliability and competitive power market issues are inevitably intertwined and there is no way to separate them. FERC has the authority to address reliability issues and DOE should encourage FERC to do so by initiating a rulemaking. Industrial Consumers offer the following comments:

- FERC has the authority and the duty to address a series of market power abuses and market barriers that impede competition and affect reliability. This authority arises under Sections 205 and 206 of the Federal Power Act.

FERC stated in Docket PL98-3, 63 Fed. Reg. 1453 (Jan. 9, 1998), that it had authority under Section 205 to address reliability rules with which customers must comply in order to obtain jurisdictional transmission services:

Historically, the Commission has followed a “rule of reason” approach and not required each contract or practice that affects a jurisdictional service to be on file, even though section 205 of the Federal Power Act may lead to that result. If the new reliability rules become terms and conditions with which customers of Commission-jurisdictional utilities must comply as a predicate to obtaining transmission service, the Commission may need to reassess how it is applying the “rule of reason.” If jurisdictional services can be denied or compromised under the new reliability rules, then section 205 appears to require that such rules be included in the transmission tariffs on file with the Commission.

Process for Assuming Non-discriminatory Transmission Service as New Reliability Rules are Developed for Using the Transmission System, 63 Fed. Reg. 1453, 1454 (Jan. 8, 1998) (emphasis added). It is clear that FERC has authority to address “service-affecting reliability practices” in the context of assuring non-discriminatory transmission access. FERC correctly stated its statutory commitment in January 1998:

**The Commission is committed to ensuring that competitive developments in the industry take place in a manner that safeguards the reliability of the nation’s electric transmission system. The Commission is equally committed to ensuring that the rules and practices for reliable operation of the grid are compatible with open, non-discriminatory use of transmission systems.**

Id.

Section 206 of the Act — which provided the factual predicate for FERC’s open access and RTO rulemakings (Order 888 and Order 2000) — further requires that FERC address impediments to reliability and competition. In Order 2000, FERC concluded that “economic and engineering inefficiencies and the continuing opportunity for undue discrimination are impeding competitive markets.” Regional Transmission Organizations, 65 Fed. Reg. 810, 825 (Jan. 6, 2000) (Order 2000).

There is a reality and a perception of anticompetitive behavior related to transmission access in the guise of reliability. The findings that FERC has made in Order 2000 and the most recent evidence provided in FERC Staff’s insightful review of the problems in Regional Power Markets<sup>1</sup> provide this factual predicate. For example, FERC Staff finds that “[a]s a result of the lack of standardized procedures for calculating ATC and CBM, and the inaccurate posting of ATC, market participants cannot determine what transmission capacity is available so that they can make deals to provide energy to their customers. This has an effect on the amount of transactions and is a limit on liquidity. . . . The dramatic 472 percent increase in TLRs between the summer of 1999 and the summer of 2000 poses a definite problem for transmission access in the Midwest. . . .” FERC Staff Investigation of Bulk Power Markets: Midwest Region, pp. 41, 47.

- Industrial Consumers recommend specific steps to address these concerns:
  - (i) Independent calculation of available transmission capacity;
  - (ii) Independent security coordinators; and

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<sup>1</sup> Investigation of Bulk Power Markets, November 1, 2000.

(iii) Requiring utilities to utilize the OATT for native load service.

- FERC cannot delegate reliability factors to NERC because it has no statutory authorization to do so. Private bodies may not be delegated regulatory functions unless (i) a statute authorizes function of the self-regulatory organization (SRO); (ii) the body is independent and complies with the process; and (iii) there is adequate agency oversight of enforcement and rulemaking functions.

- Legislative proposals to set up a new “NAERO” must avoid balkanization of power markets by vesting regional NERC councils with authority over the bulk power grid. With the advent of RTOs, there is a need to redesign proposed delineation of functions between and among RTOs, NAERO, and current regional reliability councils which is reflected in the Comprehensive Electric Competition Act (CECA) legislative proposal. Industrial Consumers propose a new delineation of functions between NAERO, regional reliability councils and RTOs in light of today’s electricity markets.

- Parochial state oversight of transmission poses a significant threat to reliability. It is critical that FERC have unequivocal statutory authority over transmission to avoid parochial decisions with respect to the bulk power grid where one state tries to favor its native load at the expense of another state’s customers.

- Given the small size of proposed RTOs, DOE should urge FERC to provide more detailed guidance on “seams issues.” Order 2000’s Function 8 addresses the need to rationalize problems at the “seams,” i.e., at or across the boundaries between adjacent RTOs, with the broader objective of Order 2000 and industry reliability standards.

While the goal of Function 8 is laudable, Function 8 does not spell out how interregional coordination is to be achieved. As a result, few of the RTO compliance filings showed meaningful steps towards interregional coordination. Most of the RTO proposals filed on October 16, 2000 reflect a failure either to expand geographic scope or to go beyond inchoate cooperative agreements. FERC cannot rely on vague promises to cooperate in the development of solutions to seams issues. Therefore, ELCON, the Electric Power Supply Association (EPSA), Enron Power Marketing, Inc., Reliant Energy Power Generation, Inc. and Dynegy Inc. recently petitioned FERC to convene a technical conference on Function 8. DOE's rulemaking should require that FERC convene a technical conference to fill in the blanks with respect to urgently-needed resolution of seams issues.

Industrial Consumers respond to the specific questions posed by DOE as follows:

1. *Is the existing arrangement of voluntary compliance with industry reliability rules sufficient to ensure reliability of the bulk power transmission system? If not, why not, and has reliability been jeopardized by violations of the existing bulk power reliability standards?* No. The main problem is that transmission owners are allowed to operate under a hodge-podge of transmission-related rules, and can selectively choose which rules to enforce depending upon a potential competitive advantage.

2. *What can FERC do under existing authorities to address reliability concerns?* Any NERC operating policy that can result in undue discrimination or other anticompetitive effects should be made part of the OATT and therefore subject to the same section 205 and 206 mandates as other terms and conditions of transmission

service. Moreover, all reliability requirements, practices and policies should be filed with FERC, provided that they affect a jurisdictional service or charge.

3. *If FERC has the authority to establish and enforce reliability standards, may FERC delegate such authority to a self-regulating reliability organization? Should it do so?* FERC cannot delegate such authority to NERC or any “self-regulating reliability organization” absent federal legislation.

4. *Are there elements in CECA [the Comprehensive Electricity Competition Act, H.R. 1828 and S. 1047], or other electric reliability legislative language, which can, with or without modification, be used in a rulemaking?* No. Legislation should establish the legal underpinnings for an Electric Reliability Organization like NAERO. Industrial Consumers recommend that the legislation should establish an Electric Reliability Organization that is charged with formulating reliability standards and policies, which would be implemented by RTOs. Regional variances should be minimal, if they exist at all.

5. *What should the relationship be between Regional Transmission Organizations, as advanced in FERC Order No. 2000, 65 FR 809 (January 6, 2000), FERC Stats. & Regs., ¶ 31,089 (2000), and an Electric Reliability Organization as proposed in CECA?* Assuming enactment of CECA or similar legislation containing the consensus reliability language, the ERO would set and enforce standards, and RTOs would implement the standards. Both the ERO and RTOs would be subject to FERC oversight.

6. *How should the responsibilities and roles of FERC and the States be addressed in a rulemaking?* The rulemaking should clarify that FERC has jurisdiction over both bundled and unbundled transmission services, including rates, terms and conditions of such services.

7. *Recognizing the international nature of the interconnected transmission grid, how could implementation of mandatory reliability standards be coordinated with Canada and Mexico?* Industrial Consumers see no insurmountable barriers to the establishment of uniform reliability standards in North America as long as there is no perception on either side of a border that a national, provincial, or state government is acting to preserve market power of incumbent interests.

#### COMMENTS

I. The Barriers To Reliability And Efficiency Are Known And Can Be Addressed By FERC Under Its Section 206 Authority

Industrial Consumers will begin by discussing major impediments in addressing reliability and then discuss FERC's authority to correct such deficiencies under existing statutory authority. Industrial Consumers will demonstrate that significant barriers to reliability and efficient competition exist and that FERC has adequate authority to remedy such barriers under its Section 206 authority.

A. FERC Staff's Recent Reports Identify Barriers To Reliability And Effective Competition

There presently exists substantial barriers to reliable, efficient and competitive

markets. FERC has unequivocally identified many such impediments to competition and reliability that must be addressed.

In the following sections, we quote extensively from FERC's November 1, 2000 Staff Reports on Regional Power Markets to provide examples of the more egregious errors.

1. FERC's Staff Report On The Midwest Markets

TLRs

“The increased incidences of TLRs [472% between the summer of 1999 and the summer of 2000] appear to have eroded confidence in the Midwest transmission market. Some public power market participants indicated to Staff that the large number of TLRs harmed the liquidity of the market by stifling long-term transactions (2-3 years). They alleged that marketers are less willing to enter into multi-year contracts for fear that they will be unable to fulfill their commitments because of the TLRs.”

“[T]here has been no concerted regulatory effort to date to police the implementation of TLRs to ensure that they are utilized properly and in a non-discriminatory fashion.”

“[T]he large number of TLR curtailments inhibits the Midwest market by preventing load from reaching its destination and by discouraging public power market participants from entering into long-term transactions. These problems will continue until TLRs become less frequent.”

Abuses of the Transmission Grid

“Several market participants have argued to Staff that the current regulatory environment has not kept up with the new challenges of the Open Access era, in which there are economic incentives for transmission providers to misuse the transmission grid to benefit their own load.”

“While a Cinergy-type situation is a cause for concern, market participants in the Midwest appear to be more concerned with setting and enforcing uniform standards for calling TLRs, and providing an effective remedial mechanism when TLRs are improperly implemented. TLRs are not called uniformly and consistently over this big physical area . . . For example, a Level 5 TLR in SPP on May 12, and again on May 16, 2000, did not curtail network services or reduce native load, it only curtailed firm point-to-point transactions.”

“The lack of uniform standards for implementing TLRs creates an uncertainty for public power market participants as to the likelihood that their transmission schedules will be curtailed. Moreover, Staff was unable to analyze, because of inadequate existing information, whether TLRs have been implemented to advantage a transmission provider’s generation resources. The lack of adequate remedial measures if this occurs appears to have crated an atmosphere of skepticism among public power market participants, who question whether transmission providers have any incentive not to use TLRs to favor their own generation.”

*Lack of Posted Information On TLRs and Curtailments*

“Another area of uncertainty for market participants relating to TLRs is the lack of information available on OASIS, particularly real-time information, concerning TLRs. Most OASIS nodes do not show curtailment amounts for each TLR. Those nodes that do list curtailment amounts do not show it for every TLR event. For instance, the top five TLR events in each of the four NERC regions for the summer of 2000 consist of 191 individual TLR events. However, 78 of those instances do not show any curtailment amount which would allow market participants to monitor if more curtailments are occurring than necessary. . . .”

“The NERC Web site does not show all TLR events or complete information on each TLR event that it does list. . . . One market participant reported that a transmission provider denied a scheduling request because the transmission provider had called a TLR. The respondent could not find any evidence that a TLR had been called either on the NERC web site or the transmission provider’s OASIS site. Another market participant provided an audio tape to Staff containing discussions with a transmission provider and other affected parties concerning a TLR that had been improperly implemented, causing the market participant a substantial financial loss.”

*Lack of Standardized Protocols for Calculating ATC and CBM and Handling Transmission Requests and Scheduling*

“There are no consistent rules for calculating and posting ATC and CBM. . . . Transmission providers have wide latitude to use various methodologies to calculate ATC. This variance comes about from different assumptions about reliability, dissimilar engineering approaches and a host of historical and operational parameters. The result is that ATC may be calculated differently on two sides of an interface. This appears to be an issue with the existing regulations, which do not provide for specific methodologies for calculating ATC and CBM.”

“ATC is often inaccurately posted on the OASIS even if calculated under the standard for the utility posting the ATC. Several market participants alleged that certain transmission providers in the Midwest were not accurately posting ATC. One market participant alleged that transmission providers in the Midwest regularly post incorrect amount for ATC and documented three examples.”

“[T]here is a lack of uniformity in processing transmission requests and scheduling service. . . . For example, reservations are not handled the same way across the entire Midwest. MAPP uses an e-mail procedure while the other three regions use OASIS sites. Two market participants complained that transmission providers are able to change their ‘Business Practices’ on the OASIS sites with little or no notice. One of those market participants alleged that this is particularly a problem with regard to next hour service, which is not covered by the OATT, but which is a major source of business for marketers and can be a source of quick response power. One market participant complained of a unilateral change by a NERC region that limited the quantity of requests that could be made to certain delivery points within a certain time.”

“One market participant noted that a particular transmission provider waits until the end of the day to accept or deny requests for next-day service, instead of making decisions as requests are made on a first-come first-served basis. As a result, the market participant stated that it did not have the flexibility to alternate deals if its request was wholly or partially rejected.”

### *Allegations of Market Power and/or Non-Competitive Behavior*

“Entities with network service have built-in advantages to service their native load over non-network (point-to-point) service. The advantages that network service have over point-to-point service are priority of service under the OATT (which has separate provisions for network service and point-to-point service), lack of curtailment until a TLR Level 5 is called, and the lack of source/sink requirements. . . . This places any NUG at a competitive disadvantage vis-a-vis the vertically integrated utilities.”

“In addition to the inherent advantages for transmission providers relating to network service under the current regulations, several market participants raised allegations of incidences in which individual transmission providers engaged in non-competitive discriminatory conduct. One market participant raised specific allegations concerning two utilities in the Midwest, alleging that they had discriminated against it by approving or confirming later affiliate requests before the market participant’s own requests, and provided supporting documentation. Three other market participants also raised allegations of transmission providers favoring their merchant affiliates. Enforcement staff is evaluating the information presented with these allegations.”

## 2. FERC’s Staff Report On Southeast Markets

“Like the Midwest, the Southeast is dominated by vertically integrated utilities that maintain substantial generation resources to serve their respective native loads. These utilities have weak economic incentives to provide transmission access to non-affiliated merchants on the same basis as they do to their affiliated merchants.”

“In general, market participants identified several inefficiencies that are frustrating the development of the bulk power markets in the Southeast. Chief among

these are uncertain transmission access, the inconsistent and apparently aberrant posting of ATC and concerns that ATC is sometimes withheld, and the lack of transparency regarding implementation of TLRs. A central theme pervading these concerns is that there is a lack of current, reliable information available to the market.”

“[M]arket participants appear to have less confidence in the Southeast market, in terms of the ability to conduct wholesale transactions without discrimination, than market participants have in other regions of the country. This lower degree of confidence appears to be justified based on investigations that the staff has undertaken and its evaluation of other complaints. Market participants’ reduced confidence weighs heavily on the maturation of markets into competitive zones of enterprise because it discourages the investment and participation needed to spur this development. The widespread perception that non-IOU entities do not receive treatment equal to that of IOU-affiliated entities frustrates the Commission’s open access goals.”

### Transmission Access

“Staff’s investigation of interconnection issues revealed that procedures governing utilities’ performance of interconnection studies are often unclear. Adherence to schedules that are established early in the interconnection request process would reduce the increasingly adversarial climate in which interconnection requests are evaluated. The time periods chosen to evaluate requests should reflect a reasoned approach to the technical challenges posed by the request and respect for the IPP’s often pressing need for promptness and certainty.”

“In one case, typical of other complaints staff received, an IPP reported that a utility quoted a period of 11 months to complete the first of several anticipated system impact studies. In the absence of an explanation that cites the technical reasons why such a period is required, 11 months to perform a system impact study appears excessive. Studies that are not promptly commenced and linger over many months cease to be commercially reasonable. . . .”

“The Commission has expressed its sympathy for the difficulties IPPs face when they seek to site a generation plant amid the uncertainty of transmission access. The staff investigation found evidence that the right of vertically integrated utilities to reserve transmission capacity has been used to deter merchants from siting plants in their respective service territories. Utilities have reserved transmission capacity in the name of serving load growth many years out, effectively deterring IPPs from siting plants in affected areas. In this connection, several IPPs complained that a utility reserved transmission capacity shortly after each IPP approached the utility with plans to site generation. According to these complaints, the utility’s reservations enormously

complicated, or precluded the IPPs from reserving point-to-point transmission service necessary to permit the planned project to go forward.”<sup>2</sup>

### ATC Issues

“As the Midwest report points out, uniform rules do not exist for calculating and posting ATC. Inconsistent and aberrant ATC postings have posed difficulties to market participants in other regions in the country and the Southeast is no different in this respect. A particularly troubling pattern occurs when a marketer enters a request for transmission service on OASIS based on the ATC posted there; the request is denied, followed by a large reduction in the posted ATC.<sup>3</sup> . . . [T]he marketer is often left to wonder what happened, as it scrambles to secure an alternate arrangement. In sum, ATC postings that are not fairly representative of actual transmission capacity and that fluctuate for no apparent reason discourage, and raise the costs of, buying and transmitting power in the bulk power market.”

### TLR Issues

“The Southeast experienced a 354-percent increase in TLRs in the summer of 2000 over the summer of 1999. . . . The high incidence of TLRs reduces certainty in the market because it frustrates the expectations of bulk power sellers and their customers.”

### Unreliable ATC/TTC

“A major problem for the markets in the Southeast is lack of information. . . . [I]n a staff audit of OASIS sites a number of problems were found. First, for both constrained and unconstrained transmission paths, ATC and TTC are often posted late, if at all. . . . [M]arket participants seldom have sufficient information concerning the precise calculation of ATC and TTC to determine whether particular postings are fair and accurate, and what ATC may be posted in the future. In addition, curtailments and the reasons for curtailing or for denying transmission service were not always posted as OASIS requires. There also were problems obtaining or downloading information concerning transmission service schedules, transmission requests and services, products and pricing, and tariffs. Moreover, several OASIS audit logs, which are used to record data and activity on the OASIS site, are not operating correctly and erase historical data so that it is impossible to audit the sites.”

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<sup>2</sup> A recent Commission decision suggests some of the problems associated with transmission reservations that IPPs face when seeking to site new generation. SkyGen Energy LLC v. Southern Company Services, Inc., 92 FERC ¶ 61,120, 2000.

<sup>3</sup> “During its recent audit of OASIS sites, staff observed this phenomenon. This audit, which is referenced in the Midwest report, determined compliance with the OASIS posting requirements of section 37.6 of the Commission’s regulations.”

B. FERC Has The Authority To Address These Problems Under Section 205 And 206 Of The Federal Power Act

1. Section 205 Authority

FERC's Section 205 authority can and should be utilized to require filing of transmission-related reliability standards. The Federal Power Act gives FERC authority over transmission rates and charges and the practices that affect such charges. Section 205(c) states:

Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classification, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

16 U.S.C. § 824d(c). Section 205(a) provides that:

All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

16 U.S.C. § 824d(a).

2. Section 206 Authority

Similarly, FERC has authority under Section 206 to ensure that “any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification” is just and reasonable and not unduly discriminatory. 16 U.S.C. § 824e(a). In Order 2000, FERC

acknowledged that “[i]n fulfilling its responsibilities under FPA sections 205 and 206, the Commission is required to address, and has the authority to remedy, undue discrimination and anticompetitive effects. The Commission has a statutory mandate under these sections to ensure that transmission in interstate commerce and rates, contracts, and practices affecting transmission services, do not reflect an undue preference or advantage . . . and are just, reasonable, and not unduly discriminatory or preferential.” 65 Fed. Reg. 810, 840.

When reliability issues affect rates and encourage discrimination FERC has authority to regulate reliability standards under section 206 of the FPA. In Order 2000, FERC recited a long litany of complaints of anticompetitive conduct:

The complaints generally involved: (1) Calculation and posting of ATC in a manner favorable to the transmission provider; (2) standards of conduct violations, (3) line loading relief and congestion management, and (4) OASIS sites that are difficult to use.

65 Fed. Reg. at 818.

FERC concluded that:

[V]ertically integrated utilities have the incentive and the opportunity to favor their generation interests over those of their competitors. If a transmission provider’s marketing interests have favorable access to transmission system information or receive more favorable treatment of their transmission requests, this obviously creates a disadvantage for market competitors.

Id. at 824.

Fears of discriminatory treatment can adversely affect competition and reliability:

[P]erceptions of discrimination are significant impediments to competitive markets. Efficient and competitive markets will develop only if market participants have confidence that the system is administered fairly. As stated by NERC, there is a reluctance on the part of market participants to share operational real-time and planning data with transmission providers because of the suspicion that they could be providing an advantage to their affiliated marketing groups, and this can, in turn, impair the reliability of the nation's electric systems. Lack of market confidence may deter generation expansion, leading to higher consumer prices. Fears of discriminatory curtailment may deter access to existing generation or deter entry by new sources of generation that would otherwise mitigate price spikes of the type that have been experienced during peak periods in the last two summer peak periods. Mistrust of ATC calculations will cause transactions involving regional markets to be viewed as more risky and will unnecessarily constrain the market area, thereby reducing competition and raising prices for consumers.

Id.

FERC made findings as to the existence of discrimination that provide the requisite predicate for FERC to address the problems that the markets are experiencing.

We also cannot dismiss the significance of reports of undue discrimination simply because they are not reduced to formal complaints. . . . [T]he cost and time required to pursue legal channels to prove discrimination will often provide an inadequate remedy because, among other things, the competition may have already been lost. . . . [C]laims of undue discrimination have not diminished, and there is no evidence that discrimination is becoming a non-issue.

Id.

## II. Positive Steps That FERC Can Take To Solve The Problems

In light of the experience of Market Participants and the findings of the November 1, 2000 FERC Staff Report, it is evident that several immediate corrections are needed to create competitive markets and improve reliability.

A. DOE Should Insist On Independent Calculation And Posting Of ATC

ATC and OASIS do not provide market participants with meaningful information about how the system was being used and how it could be used. The result has been far less than satisfactory.

Order No. 2000 provides that RTOs will calculate the ATC values based on data developed partially or totally by the RTO, thus ensuring that “ATC values are based on accurate information and consistent assumptions.” Id. at 898.

Prior to implementation of Order 2000, FERC could require transmission owners to have an independent firm calculate ATC. In American Electric Power/Central Southwest, 90 FERC 61,242 (2000), FERC required that ATC valuation be performed by an independent entity prior to the formation of an RTO. AEP/CSW provides useful precedent that independent calculation of ATC can address concerns raised about manipulation of ATC calculations and service denials by transmission owners.

FERC’s November 1, 2000 Report on Regional Power Markets points out the problems with OASIS posting and improper implementation of FERC policies and NERC procedures. At a minimum, DOE should encourage FERC to audit key information on OASIS, including ATC.

B. Independent Security Coordinators Are A Necessity

As FERC Staff stated in the November 1, 2000 Report on Southeast Power Markets:

Whether security coordinators are truly independent and do not favor their employer-utility has been questioned. As in the case of interconnection access, the built-in incentive to favor use of the incumbent utility's assets colors the perception of impartiality of security coordinators in the implementation of NERC's TLR criteria. Staff has not confirmed that any bias that may exist has been exercised in any specific instance to the detriment of a market participant, but it cannot discount the possibility that the force of economic incentives may play a role in TLR implementation.

FERC Staff Investigation of Bulk Power Markets: Southeast Region, p. 49.

In Order No. 2000, FERC recognized "the independence of the Security Coordinator is important for ensuring non-discriminatory transmission service and the RTO will have that independence." 65 Fed. Reg. at 867.

Security Coordinators inevitably are apprised of highly commercially-sensitive information about system operations, schedules and reservations. While NERC has adopted a code of conduct, this is a behavioral rather than a structural remedy. As Federal antitrust authorities have repeatedly cautioned, in the area of transmission access, subtle delays in responding to transmission requests are impossible to monitor.<sup>4</sup> It is far too easy for Security Coordinators to favor their affiliated merchant function and far too difficult to police that conduct to ensure that Security Coordinators are, in fact, operating the system fairly and in a non-discriminatory manner.

In Order 2000, FERC observed that codes of conduct have not been sufficient to deter improper behavior:

While we have attempted to rely on functional unbundling to address our concerns about undue discrimination, there are indications that this is difficult for transmission providers to

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<sup>4</sup> See Dkt. Nos. EL00-95, RM99-2, Comments of the Staff of the Bureau of Economics and of Policy Planning of the Federal Trade Commission.

implement and difficult for the market and the Commission to monitor and police. In cases in which the Commission has issued formal orders, we have found serious concerns with functional separation and improper information sharing with respect to at least four public utilities. In addition, our enforcement staff is receiving an increasing number of telephone calls about standards of conduct issues, ranging from simple questions about what is permissible conduct to more serious complaints alleging actual violations of the standards of conduct. In a number of cases, our staff has verified non-compliance with the standards of conduct.

65 Fed. Reg. at 824

The forced revelation of proprietary commercial relationships is antithetical to a competitive market. Transmission tags are provided to the Security Coordinators, who in many cases are also control area operators. FERC's Staff Report on the Midwest Market Notes that: "[s]ome market participants have suggested that the increased incidents of TLRs, in many instances, are the result of noncompetitive behavior by vertically integrated transmission providers to benefit their affiliates." FERC Staff Investigation of Bulk Power Markets: Midwest Region, pp. 42-43 (citing "Transmission Markets, Stretching the Rules for Fun and Profit," Narasimha Rao and Richard D. Tabors, TCA Working Paper No. 327-0400, April 2000). Because the Security Coordinator, who calls TLRs, often works for an integrated IOU, there exists a mixed incentive to enforce reliability on the grid and to maximize profit for the IOU.

Security Coordinators have no contractual relationship with Transmission Customers, such as would provide such customers with a straightforward legal remedy for economic injury caused by breach of duty. Where the Security Coordinator is also a transmission-owning utility, tagging vests it with superior knowledge of competitively-

priced energy at the same time that the all-powerful Security Coordinator has the authority to make the critical decisions to resolve a claim of transmission congestion.<sup>5</sup>

To avoid such discrimination, DOE's rulemaking should require that the Security Coordinators operate independently of the Transmission Providers as soon as possible.

At a minimum, the FERC Staff Report suggests an urgent need for development of auditable data. Such data would disclose system conditions existing at the time of a TLR to confirm that all applicable rules and procedures were properly observed.

C. Native Load Must Be Served Under The Same Tariff Provisions As Other Transmission Customers

FERC's Staff Report on the Midwest markets recommends that FERC:

reduce the advantages of network service over point-to-point service by requiring that native load be served under the same tariff provisions as other transmission services. Given that all transactions serve load of one sort or another, all load would be treated in the same manner. This would eliminate the current incentives that vertically integrated transmission owners have to favor their native load through the manner and method of calculating ATC and handling interconnection requests. It would also restore confidence among market participants that transmission owners were not calling TLRs to favor native load, because they would no longer have the incentive to do so.

FERC Staff Investigation of Bulk Power Markets: Midwest Region, p. 57. The Staff

Report finds:

[M]any vertically integrated transmission owners may have incentives to resist efforts to make this information transparent and standardized, including information on the manner in which "native load" is handled in making these calculations. These incentives would also exist for transmission owners belonging to RTOs which allow them to individually calculate, or provide

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<sup>5</sup> Through tagging, all the Transmission Providers know the source of supply, as well as all the wheeling transactions being utilized.

information to assist in calculating, ATC. As a consequence, the Commission may wish to eliminate the native load exemption and have all transactions under the same tariff. Given that all transactions serve load of one sort or another, all load would be treated in the same manner. This would provide all transmission owners the proper incentives to make relevant information available.

Id. at 49.

Since March 1998, Industrial Consumers, Enron and other allies have advocated that FERC conduct a rulemaking to assure that transmission providers are required to provide service to native load customers under the *pro forma* tariff.<sup>6</sup> The Commission's open access rules apply to less than twenty percent of transmission service. Because bundled service remains shielded from any OASIS posting or other public disclosure, the ability to game the system is virtually unlimited and, worse, impossible to detect or prove. Only when all uses of the system occur under the requirements of the tariff, will market participants have any confidence that the system is being used fairly and comparably.

The elimination of residual discrimination will occur only when all uses of the transmission grid are under the same rate schedules, terms and conditions. With actual comparability, the transmission owner's interest would be to operate the grid as a stand-alone business and maximize throughput, rather than to use transmission to favor the transmission owner's generation, marketing and sales. Comparability is critical if competitive power markets are to achieve their full potential and ensure reliability.

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<sup>6</sup> On March 25, 1998 ELCON, APX, Inc., and a group of power marketers and IPPs filed a petition with FERC for a rulemaking that would rectify this problem. FERC never acted on the petition. See Petition for a Rulemaking on Electric Power Industry Structure and Commercial Practices and Motion to Clarify or Reconsider Certain Open-Access Commercial Practices, Dockets No. RM95-8-000 & RM98-5-000.

D. There Must be Specific Guidance And A Specific Timetable For Interregional Implementation Of Function 8—Interregional Coordination

In Order 2000, FERC relied on Function 8 to address the problems of too small RTOs:

We are receptive to flexible and innovative ways for an RTO to achieve sufficient scope. Where a proposed regional transmission entity may be of sufficient scope for some RTO purposes, but not others, an RTO may be able to achieve sufficient “effective scope” by coordination and agreements with neighboring entities, or by participating in a group of RTOs with either hierarchical control or a system of very close coordination. We do not foreclose the possibility that an RTO may satisfy some of the minimum characteristics and functions by itself, while satisfying others through a strong cooperative agreement with neighboring RTOs to create a “seamless trading area.” The functions of a large RTO may be met by eliminating the affect of seams.

65 Fed. Reg. at 863.

Given FERC’s decision to date not to mandate RTO boundaries,<sup>7</sup> effective resolution of seams issues is critical: (i) to increase commercial activity between and

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<sup>7</sup> FERC has authority to establish boundaries for RTOs pursuant to DOE’s October 7, 1998 delegation of authority to FERC, 63 Fed. Reg. 53,889.

Section 202(a) of the Federal Power Act provides DOE with sufficient authority to establish boundaries for Independent System Operators (ISOs) or other appropriate transmission entities. DOE has not exercised this authority. However, FERC devotes substantial resources to ISO development and regulation. FERC is also increasingly faced with reliability-related issues. Providing FERC with the authority to establish boundaries for ISOs or other appropriate transmission entities could aid in the orderly formation of properly-sized transmission institutions and in addressing reliability-related issues, thereby increasing the reliability of the transmission system. The Department has therefore concluded that the Commission is the most appropriate agency to exercise authority under Section 202(a). Accordingly, the Secretary is

among regions; and (ii) to improve reliability without adverse impacts on operations or markets.

There can be little doubt about the need for immediate progress on interregional coordination.

- FERC’s November 1, 2000 Order on the “crisis” in California electricity markets attributes much of the blame to balkanization of the Western grid.
- FERC’s Chairman has deplored the absence of a single Northeast RTO.
- Reliability problems will be perpetuated or exacerbated by too small RTOs. FERC has recognized the tradeoff between Function 8 and Characteristic 2—inadequacies in geographic configuration can be mitigated by strong Function 8 compliance.
- Market power and economic efficiency—important goals of Order 2000—cannot be addressed effectively if RTOs charge transmission tolls at their borders. The geographic area for electricity trading must be broadened by either broadening the geographical reach of RTO tariffs or by rate reciprocity.

In the October RTO filings, transmission owners commit to little more than promises to get together to discuss cooperation but there are no milestones for

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delegating to the commission his authority under Section 202(a) of the Federal Power Act.

accomplishment of concrete objectives. This “push” must come from FERC or DOE.

Both agencies should insist that all stakeholders, not just transmission-owning utilities, sit at the table when elimination of seams issues is discussed.

ELCON, EPSA, Enron Power Marketing, Reliant Energy Power Generation and Dynegy have petitioned FERC to convene a technical conference to develop a specific template for seams resolution which RTOs should be required to meet.

At a minimum, issues to be addressed would include:

- Scheduling and reserving transmission (e.g. scheduling protocols, emergency procedures, curtailment, market closing times)
- Operational practices (e.g. ramp rates, definition of proxy buses)
- ATC calculation (including TTC, CBM)
- Transmission rights
- Congestion Management
- Interconnection Issues
- Ancillary services standards

FERC has established technical conferences and workshops on other topics of importance especially where the Commission wished to foster an exchange of views. Examples include regional workshops on RTO formation and technical

conferences on calculation of (i) capacity benefit margins; (ii) electronic filing; (iii) Y2K readiness; and (iv) revision to Oil Pipeline FERC Form 6.

DOE should encourage FERC to convene a technical conference or workshop to address “seams” issues and appropriate implementation of Function 8. It is important that the conference have a forward-looking focus: It is necessary to address what will be done to eliminate seams issues rather than re-hash efforts to date.

### III. Industrial Consumers’ Responses To Specific Questions In DOE’s Notice

1. *Is the existing arrangement of voluntary compliance with industry reliability rules sufficient to ensure reliability of the bulk power transmission system? If not, why not, and has reliability been jeopardized by violations of the existing bulk power reliability standards?*

The existing arrangement of voluntary compliance with industry reliability rules (including so-called *commercial practices* that also impact reliability) is not sufficient to ensure reliability of the bulk power transmission system. In fact, the exercise of market power in order to preserve an unearned competitive advantage may be the single biggest risk to grid reliability.

Transmission owners are not required to offer services relating to any physical transaction on their systems under a single, uniform, unambiguous set of regulations. As such, transmission owners that continue to serve “native load,” and also have unregulated generation, or retail or wholesale marketing affiliates, can engage in practices that in reality are disguised means of discriminating against potential competitors.

The main problem is that transmission owners are allowed to operate under a hodge-podge of transmission-related rules, and can selectively choose which rules to

enforce depending upon a potential competitive advantage. For example, one set of rules is defined by Orders 888 and 889 under the jurisdiction of FERC. However, these rules have only limited applicability. FERC has not required that a transmission owner subject itself to these rules (specifically, the rates, terms and conditions for transmission services under the pro forma open-access transmission tariff or OATT) to provide service to native load customers. Ironically, FERC has acknowledged that this shortfall can lead to the exercise of market power (or the mere perception of such power) and that FERC has adequate authority under the Federal Power Act to mitigate this exercise of market power.

Another set of rules is under the de facto “jurisdiction” of NERC. These rules are NERC’s operating and planning policies for maintaining the reliability of the interconnected transmission systems. NERC also promulgates certain commercial practices. Some of these commercial practices are required by FERC and subject to FERC approval (e.g., OASIS business practices), but others are not. NERC cannot enforce its policies and therefore transmission owners are generally free to implement these requirements on an *a la carte* basis, often for reasons not intended by NERC. For example, NERC’s Transmission Line Loading Relief (TLR) Procedures were intended to be used as a last resort to avoid blackouts. Instead, TLRs are increasingly used as a congestion management tool whereby a transmission owner can cut a competitor’s transactions to free-up space on the system for the owner’s transactions. Practices relating to Capacity Benefits Margin (CBM) and the calculation of TTC and ATC are used the same way.

2. *What can FERC do under existing authorities to address reliability concerns?*

Any NERC operating policy that can result in undue discrimination or other anticompetitive effects should be made part of the OATT and therefore subject to the same section 205 and 206 mandates as other terms and conditions of transmission service. FERC's authority over the use of the transmission system is plenary and it is inconsistent to treat NERC operating policies as non-jurisdictional. The argument that FERC does not have authority over reliability is meaningless because no one questions FERC's authority over ancillary services. In fact, NERC—which refers to ancillary services as “interconnected operations services”—calls them the “building blocks” needed to maintain the reliability of the interconnected power systems in North America.<sup>8</sup>

NERC guidelines and standards that affect the provision of transmission and ancillary services clearly are practices significantly affecting jurisdictional rates and charges, and therefore are subject to the Commission's jurisdiction under Section 205(c).

The statutory directive [of Section 205(c)] must reasonably be read to require the recitation of only those practices that affect rates and services significantly, that are realistically susceptible of specification, and that are not so generally understood as to render recitation superfluous.

Public Service Co. of Colorado, 67 FERC ¶ 61,371 at 62,267 (1994) (quoting City of Cleveland v. FERC, 773 F.2d 1368, 1376 (D.C. Cir. 1985)) (emphasis in original).

All reliability requirements, practices and policies should be filed with FERC, provided that they affect a jurisdictional service or charge. In reviewing a particular

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<sup>8</sup> North American Electric Reliability Council, *Policy 10 – Interconnected Operations Services*, Draft 3.2, October 11, 2000, page P10-4.

standard and deciding whether to impose it in a transmission tariff, the Commission must consider (a) whether the standard serves a legitimate reliability purpose, (b) whether the standard, in combination with other standards, is sufficient to ensure reliability, and (c) whether the standard is anti-competitive or discriminatory.

As noted above, Section 206 also provides a mandate for FERC to address reliability rules. There are many rules and requirements that a reliability council, typically controlled by transmission owners, may adopt to favor the owners' loads and resources and use of the grid. In an increasingly competitive environment, the temptation to do so can be very strong. The Commission must assert jurisdiction to ensure that the Federal Power Act's non-discrimination purposes are not undermined in the guise of protecting reliability. If FERC has authority over interstate transmission, necessarily it must have authority over transmission practices that reflect transmission access (ATC, TTC, CBM, and TLR).

3. *If FERC has the authority to establish and enforce reliability standards, may FERC delegate such authority to a self-regulating reliability organization? Should it do so?*

FERC cannot delegate such authority to NERC or any "self-regulating reliability organization" absent federal legislation.

*Why FERC Cannot Delegate Authority To Set Reliability Standards to NERC*

- (i) Absent Statutory Authorization, Reliability Authority May Not Be Delegated To A Private Body-Especially A Body That Is Not Independent

NERC represents an exceptional instance where regulatory authority has implicitly been delegated to a private standard-setting organization. Even express

statutory delegations of law-making power to private organizations are “especially suspect.” Davis, Administrative Law, § 1.3.2. In Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935), the Supreme Court invoked the anti-delegation doctrine to strike down the National Recovery Administration. Conveying authority to private associations to formulate their own “codes of fair competition” is suspect because such associations may protect themselves at the expense of customers and consumers. See Schechter Poultry Corp., 295 U.S. at 537.

Delegation to private bodies is “delegation in its most obnoxious form; for it is not even delegation to an official or an official body, presumptually disinterested, but to private persons whose interests may be and often are adverse to the interests of others in the same business.” Carter v. Carter Coal Co., 298 U.S. 238, 311 (1936). Even in cases of express statutory delegation of authority to a private body, which NERC does not currently enjoy, courts have overturned delegation of unfettered power to private agencies. See Washington ex rel. Seattle Title Trust Co. v. Roberge, 278 U.S. 116 (1978); Grendel’s Den v. Goodwin, 662 F.2d 88, 92-93 (1<sup>st</sup> Cir. 1981); State Board of Dry Cleaners v. Thrift-D-Lux Cleaners, 254 P.2d 29, 36 (Cal. 1953).

In case law involving NASD and the Maloney Act, the courts upheld Congressional delegation of legislative power to a private institution. See Todd and Co. v. SEC, 557 F.2d 1008 (3d Cir. 1977); R.H. Johnson & Co. v. SEC, 198 F.2d 690 (2<sup>nd</sup> Cir. 1952) (finding that the Maloney’s Act’s delegation of authority to a private body was constitutional where the Commission (1) had the power, according to reasonably fixed statutory standards, to approve or disapprove the association’s rules; (2) must make de novo findings and (3) provided a full review of the association’s decision).

(ii) FERC Is Excessively Deferential To NERC Which Has Not Transformed Itself Into An Independent Entity

Without extensive FERC oversight, NERC exercise of regulatory power is not only ill-advised as a policy matter, but would constitute an unconstitutional delegation of FERC's authority. Given the lack of independence of subgroups and other committees engaged in the NERC standard-setting impact and the undeniable impact of actions such as Policy 3 on competitors, vigilant FERC oversight is essential.

NERC has presented legislative language to Congress which it has requested be considered in connection with statutory establishment of NAERO.<sup>9</sup> This language promises independence of NERC and its committees and balance and openness in its process. Yet NERC has dragged its feet in restructuring its own operations to adopt the due process and independence features that it has committed to follow when NAERO is established. NERC wants the deference that is due to an independent SRO before it has adopted the independent governance and due process procedures that NASD and other SROs have adopted. Industrial Consumers believe that it is entirely inappropriate for FERC to continue its policy of deference to NERC which is exercising quasi-regulatory authority de facto until it meets the NAERO procedural safeguards espoused by NERC in its legislative proposal.

Before it is entitled to any deference, NERC should reform itself by the elimination of the Regions' strangle-hold over NERC operations, the institution of a truly independent board, and the development of a new interim bylaws that adopt the full panoply of due process procedures.

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<sup>9</sup> See Consensus Legislative Language Approved by NERC Board of Trustees, Feb. 1, 1999.

NERC is not independent in its board membership, or in its committee structure. While NERC has moved in the direction of balance by dividing committees into “transmission owners” and “transmission customers” the current committee membership remains out of balance and out of sync with changes in the corporation of the market place. For example, the current committee structure does not allow voting membership of RTOs, ISOs, PXs, APX or other new entities participating in the market. It would be folly to adopt a regime that allows NERC to develop standards that offered transmission when it does not have an independent governance structure when FERC has recognized that independence is an essential characteristic for RTOs and ISOs.

(iii) Reform Will Lessen The Likelihood That NERC Activities Will Cause Or Be Alleged To Cause Anti Competitive Injury

As the FTC Bureau of Consumer Protection stated in its “Final Staff Report on Standards and Certification” in April 1983:

Participants in the process have an opportunity (through the standards development committee) to collude to injure competition through lessening competition among themselves or through injuring other competitors, as well as the means (through the resulting standard) to effectuate any anticompetitive conspiracies. The use of the standards development process with the purpose of achieving an unlawful restraint constitutes an unfair method of competition.

at 276.

Standard-setting organizations perform valuable functions but many of their endeavors elicit challenges that actions taken may impair competition. Antitrust review focuses on the fairness of process used in developing standards and whether standards that are developed are intended to prevent competing suppliers from introducing lower-cost products and services. See Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988); American Society of Mech. Engineers (“ASME”) v. Hydrolevel Corp.,

456 U.S. 556 (1982); Session Tank Lines, Inc. v. Joor Mfg. Inc., 786 F. Supp. 1518, rev'd, 17 F.3d 295 (9<sup>th</sup> Cir.).<sup>10</sup>

Various aspects of NERC's rules and policies are controversial and can trigger challenge by competitors. While legislation authorizing NAERO will address the role of FERC oversight and antitrust compliance with respect to NAERO participation, it is unlikely that blanket antitrust immunity will be adopted. Rather, "rule of reason" analysis is likely to be applied. Accordingly, it is in the best interest of NERC, and its participants, to adopt the full panoply of due process procedures in its standard-setting process.

Properly fashioned and implemented procedural guidelines are relevant under rule of reason analysis for evaluating specific standards-related conduct. For example, the Supreme Court in Allied Tube stated that "[t]he hope of procompetitive benefits depends upon the existence of safeguards sufficient to prevent the standard-setting process from being biased by members with economic interests in restraining competition." 486 U.S. at 509. See also Pretz v. Holstein Friesian Ass'n of America, 698 F. Supp. 1531, 1540 (D. Kan. 1988) (stating that the "presence or absence of a fair hearing...certainly affects the factfinder's determination of defendant's motive or intent and reasonableness of defendant's restraints under a rule of reason analysis"); Brant v. United States Polo Ass'n, 631 F. Supp. 71, 78 (S.D. Fla. 1986) (finding that the "[p]laintiff could argue...that the lack of procedural due process or fair play...somehow evidences an anticompetitive motive and intent").

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<sup>10</sup> The district court found anticompetitive conduct in adoption of standards. While the court of appeals reversed the district court, the grounds for reversal (applicability of the Noerr-Pennington doctrine) did not reject the district court's conclusions.

The worthwhile mission of NERC -- to provide reliability -- will not protect NERC from antitrust scrutiny under rule of reason analysis. See National Society of Professional Engineers v. United States, 456 U.S. 679, 691 (1978) (engineering association's restrictions on competitive bidding justified by the association on the basis of public safety invalidated as a restraint of trade under rule of reason analysis). See also American Society of Mech. Engineers, 456 U.S. 556. NERC's failure to provide well-established due process safeguards will leave it vulnerable to antitrust challenge.

4. *Are there elements in CECA [the Comprehensive Electricity Competition Act, H.R. 1828 and S. 1047], or other electric reliability legislative language, which can, with or without modification, be used in a rulemaking?*

No. Legislation should establish the legal underpinnings for an Electric Reliability organization like NAERO. FERC should implement a rulemaking to implement the legislative mandates. The CECA contains the "consensus" language established a couple of years ago through NERC. RTOs weren't even thought about then. The "consensus" language gives substantial deference to Affiliated Regional Reliability Entities (ARREs). This deference is now outdated and should not be implemented.

NERC is not a unified, top-down organization. On the contrary, the regions exercise enormous authority and impede NERC's ability to act on important initiatives. While some regions are commendably transforming themselves into RTOs, other regions are pursuing their own agenda.

The uniform and consistent application of NERC standards and practices is essential both for reliability and commercial needs. Any inconsistent application of reliability standards within an interconnection is itself a serious threat to bulk-power reliability. Regional entities must not be allowed to unilaterally select and implement

NERC standards and practices on an *a la carte* basis. Only approved RTOs should be allowed to request any variance to a NERC standard or practice. Any regional variance must not be approved absent a showing of fact before the Commission that such a variance is consistent with or superior to the standard or practice as promulgated by NERC, and is competitively neutral with respect to interconnection-wide commercial activities.

Industrial Consumers recommend that the legislation should establish an Electric Reliability Organization (ERO) that is charged with formulating reliability standards and policies, which would be implemented by RTOs. Regional variances should be minimal, if they exist at all. This model is described further in question #5.

5. *What should the relationship be between Regional Transmission Organizations, as advanced in FERC Order No. 2000, 65 FR 809 (January 6, 2000), FERC Stats. & Regs., ¶ 31,089 (2000), and an Electric Reliability Organization as proposed in CECA?*

Assuming enactment of CECA or similar legislation containing the consensus reliability language, the ERO would set and enforce standards, and RTOs would implement the standards. Both the ERO and RTOs would be subject to FERC oversight.

In Order 2000, FERC gives RTOs the exclusive authority for maintaining the short-term reliability of the grid each RTO operates. RTOs must also serve as a provider of last resort of all ancillary services required under Order 888 and subsequent orders. In addition, every RTO must be the NERC Security Coordinator for the facilities that it controls. Thus, by reassigning the responsibilities for implementing reliability standards from the transmission owners to independent RTOs, the RTO becomes the FERC's agent

for enforcing compliance with the standards by virtue of the RTO's operational control of transmission facilities.

Perhaps more interesting (and problematic) is the relationship between the proposed *Affiliated Regional Reliability Entity* (ARRE) and RTOs, or between an ARRE and the ERO. ARREs are authorized under the consensus reliability legislation to adopt Entity Rules for a specific region that are designed to implement or enforce one or more of the ERO's Organization Standards. An ARRE may also seek a Variance (or exception) from the requirements of an Organization Standard, subject to the approval of the ERO. The intent of an ARRE, arguably, is to replicate (or preserve) the role of existing Regional Reliability Councils (RRCs) under the ERO. This is inefficient given the nature of the authorities given to RTOs by Order 2000 as codified in CECA.

The consensus reliability language was drafted without full consideration or recognition of RTOs. In fact, except for ARREs, the language was not drafted to rationalize the need for any other existing or new regional entities with some form of authority over reliability (including the planning of the transmission system). The Barton bill (HR 2944) would have sanctioned eleven regional entities compared with the five that currently exist.

## Regional Reliability Entities

### Existing and Authorized by HR 2944

Existing Regional Entities	Regional Entities Authorized by HR
<ol style="list-style-type: none"> <li>1. NERC</li> <li>2. Regional Reliability Councils (RRCs)</li> <li>3. Regional Transmission Groups (RTGs)</li> <li>4. ISOs</li> <li>5. Multi-Company Control Areas</li> </ol>	<ol style="list-style-type: none"> <li>1. Electric Reliability Organization (Section 201, would replace NERC)</li> <li>2. RRCs (Regional Reliability Councils)*</li> <li>3. ISOs (Section 103 grandfathers existing regional entities)</li> <li>4. Multi-Company Control Areas*</li> <li>5. Regional Transmission Groups (RTGs)</li> <li>6. RTOs (Section 103)</li> <li>7. Transcos (Section 103)</li> <li>8. Regional Transmission Siting Agencies (Section 104)</li> <li>9. Joint Boards (Section 105)</li> <li>10. ARREs (Affiliated Regional Reliability Entities) (Section 201)</li> <li>11. RABs (Regional Advisory Bodies) (Section 201)</li> </ol> <p>*These existing entities would be allowed to continue operating under HR 2944.</p>

The Department should consider, as part of this inquiry, a review of all the various proposals for “regional entities” and attempt to rationalize the need for such entities consistent with the needs of both the marketplace and reliability. For example, Industrial Consumers recommend an industry structure based upon the following regional entities:

Regional Entity	Responsibility
1. North American Electric Reliability Organization (NAERO)	<ul style="list-style-type: none"> <li>• Replaces NERC; develops reliability standards and commercial practices.</li> </ul>
2. Regional transmission siting agencies (or, alternatively, give siting authority to FERC)	<ul style="list-style-type: none"> <li>• Provide regulatory siting function for interstate transmission facilities; replaces state siting authority only over interstate facilities.</li> </ul>
3. Regional transmission organizations (RTOs)	<ul style="list-style-type: none"> <li>• Replace existing ISOs, regional reliability councils, and regional planning groups (RTGs). Also subsume responsibilities of Affiliated regional reliability entities in HR 2944. RTOs operate the grid to ensure nondiscriminatory access, provide congestion management services, and act as NAERO-certified security coordinator.</li> </ul>
4. Independent transmission companies (ITCs) and other transmission-owning entities (e.g., BPA, NYPA)	<ul style="list-style-type: none"> <li>• Owns transmission; operates transmission facilities as directed by RTO.</li> </ul>

6. *How should the responsibilities and roles of FERC and the States be addressed in a rulemaking?*

The rulemaking should clarify that FERC has jurisdiction over both bundled and unbundled transmission services, including rates, terms and conditions of such services. FERC also has sole authority with respect to the reliable operation of the interconnected grid, e.g., by its section 205 authority to establish ancillary services and by the relevant reliability-related requirements in Order 2000.

7. *Recognizing the international nature of the interconnected transmission grid, how could implementation of mandatory reliability standards be coordinated with Canada and Mexico?*

Industrial Consumers see no insurmountable barriers to the establishment of uniform reliability standards in North America as long as there is no perception on either

side of a border that a national, provincial, or state government is acting to preserve market power of incumbent interests.

International cooperation can be implemented either through government to government memoranda of understandings or via inter-RTO agreements. As between governments, “the memorandum of understanding is a well-accepted type of legal instrument in international law and practice.”<sup>11</sup> By expressing the intent of the parties, countries signing MOUs can indicate their intent to be legally bound. The Department of State lists numerous examples of MOUs among “treaties in force.” The United States has entered into dozens of such agreements with other countries in the area of energy, environment, antitrust and securities regulation. Post NAFTA, there has been an increase in cross-border cooperation. For example, the trilateral North American Commission on Environmental Co-operation. On the U.S.-Mexican border, a variety of economic development initiatives have been initiated (for example between Arizona and Sonora) and across the U.S.-Canadian border, economic initiatives have occurred under a self-styled Pacific Northwest Economic region.<sup>12</sup>

However, private initiatives are equally appropriate. Ontario's IMO has signed a memorandum of understanding to cooperate with the Northeast ISOs on interregional coordination. RTO West has entered into a similar initiative with British Columbia and potentially Alberta. DOE should urge FERC to require that U.S. RTOs move to

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<sup>11</sup> J. McNeill, *International Agreements: Recent US-UK Practice Concerning the Memorandum of Understanding* 88 AM. J. INT'L L. 821 (Oct 1994). McNeill was Sr. Deputy Counsel, U.S. Dept of Defense.

<sup>12</sup> For examples of cross border regional initiatives, see J. Scott, *European and North American Contexts for Cross Border Regionalism*, Regional Studies (Oct. 99) (available on Lexis).

eliminate “seams” issues with neighboring RTOs even across international borders given the need for reliability.

Industrial Consumers note efforts between sponsors of RTO West and their Canadian counterparts in British Columbia to coordinate and integrate Canadian entities into the RTO West framework notwithstanding the jurisdictional divide. Under their proposed framework, a new Independent Grid Operator in British Columbia (“BC IGO”) would be developed in parallel with the formation of RTO West. BC IGO would meet the independence standards of Order 2000, although it would be under the jurisdiction of the British Columbia Utilities Commission. The business practices for RTO West and BC IGO would be uniform and include a single OASIS site operated by RTO West. RTO West would operate a uniform congestion management procedure across all facilities controlled by RTO West and BC IGO and would also act as provider-of-last-resort for ancillary services in the greater region. A single Security Coordinator would cover both RTO West and BC IGO, and electronic data communication between RTO West and BC IGO control centers would allow them to efficiently operate in tandem.

We believe that this accommodation between RTO West and BC IGO was possible because no side had undue market power and both sides had everything to gain by cooperation.

Respectfully submitted,

/s/ Sara S. Schotland \_\_\_\_\_

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