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BEFORE THE
UNITED STATES OF AMERICA
Federal Trade Commission

Notice Requesting Comments on Retail Electricity Competition Plans	)	**V010003— Comments Regarding Retail Electricity Competition**

COMMENTS OF THE
NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

The National Association of Regulatory Utility Commissioners ("NARUC") respectfully files these comments in response to the "Notice Requesting Comments on Retail Electricity Competition Plans" ("Notice") published by the Federal Trade Commission ("FTC") at 66 Fed. Reg. 13,536 (March 6, 2001).

NARUC represents the governmental agencies of the fifty States, the District of Columbia, Puerto Rico and the Virgin Islands engaged in the regulation of public utilities and common carriers. NARUC's mission is to serve the public interest by improving the quality and effectiveness of public utility regulation. Under State law, NARUC's members have the obligation to ensure 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 that are just, reasonable and nondiscriminatory for all consumers.

NARUC appreciates the FTC undertaking to gather information regarding the results to date of different regulatory approaches to the issues that arise in restructuring the retail sale of electricity. While careful review of State restructuring activities discloses that these initiatives contain many common elements such as customer choice, functional unbundling, pricing reform, stranded cost recovery, protection of public benefits, and the like, the States that have embarked on the path of restructuring often have chosen somewhat divergent routes. As our First Vice

President, Commissioner Bill Nugent of Maine, testified before the Senate Energy and Natural Resources Committee in March, "[f]or better or worse, the States are the proving grounds for innovations in energy policy. One observation that can be made regarding State energy policy activities is that one size does **not** fit all." *To Review Current U.S. Energy Trends and Recent Changes in Energy Markets: Hearings Before the Senate Energy and Natural Resources Committee*, 107th Congress (2001)[hereinafter *Hearings*](testimony of Commissioner William M. Nugent). Commissioner Nugent's testimony is attached as Appendix A. What is important to note is that those closest to the unique conditions of electricity markets – the State commissions and legislatures -- are acting to ensure vibrant, safe and sustainable markets. A careful review of competitive electricity plans will show the importance of maintaining State flexibility.

To date, 24 States, plus the District of Columbia, are in the process of implementing retail competition laws and/or regulation. Based on the number of States moving towards restructuring and the constantly evolving nature of this industry, NARUC established an Electric Regulatory Database maintained by the National Regulatory Research Institute. That database can be accessed at http://www.naruc.whatsup.net/. That database gives historical perspectives, details State regulations, and provides commentary on pertinent issues. For specific answers to the questions posed in the Notice, the FTC may wish to access this database.

As those responsible for ensuring reliable and reasonable electrical service in the 50 States, NARUC welcomes the opportunity to contribute to the FTC's information gathering on electricity competition plans. While NARUC will defer to the comments of individual State commissions for State-specific information, NARUC has been an active participant in the formulation of policy and has commented on numerous occasions on the issues surrounding the restructuring of the electricity industry. Pertinent resolutions and comments are attached to these comments. Additionally, as noted, many of the individual States will be filing separate comments. In response to the questions posed by the FTC, NARUC comments as follows:

I. History and Overview

For most of the twentieth century, States have regulated all aspects of bundled retail electric service. As the electric power industry developed increased technical generation and transmission capability in the early part of this century, the industry was transformed from a local and urban industry into one capable of producing large amounts of power at a central location and transmitting this power vast distances. As efficiencies improved, prices declined.

The current changes in the electric industry are based on changes in energy policy and legislation initiated during the 1970s and on the regulatory innovations of the Carter Administration. The Public Utility Regulatory Polices Act of 1978 (PURPA) required electric utilities to interconnect and buy, at the utilities' avoided cost, capacity and energy offered by any non-utility facility that met certain qualifying criteria for co-generation, renewable resources or small hydro-electric facilities, as implemented by the Federal Energy Regulatory Commission (FERC). *See*, Rose, Kenneth, *United States, Restructuring of the Electric Industry*, *Industry Restructuring Initiatives*, *Source of Restructuring Initiative* (April 18, 1999), *available at* NARUC Electric Restructuring Database, http://www.naruc.whatsup.net.

The next major energy policy to impact the evolution of electricity markets, the Energy Policy Act of 1992 (EPACT), provided the FERC authority to open access to transmission networks. In addition, EPACT exempted certain non-utility generators from the restrictions of the Public Utility Holding Company Act of 1935 (PUHCA). Under the direction of the Securities and Exchange Commission (SEC), PUHCA had broken up the very extensive interstate holding companies that had developed in the early years of the 20th Century and required them to divest their holdings until each became a single consolidated system serving a circumscribed geographic area. PUHCA also permitted holding companies to engage only in business that was essential and appropriate for the operation of a single integrated utility, thereby practically eliminating the participation of non-utilities in wholesale electric power sales prior to the enactment of EPACT.

In addition to these regulatory changes in the industry, by 1994, the wholesale price of electricity had fallen dramatically because of the surplus of generation capacity. Large industrial customers in high-cost States asked their State legislatures or State commissions to allow retail customers to have direct access to wholesale markets. *See Hearings*. NARUC's guiding principle, which has been the guiding principle for many of the States that moved to restructuring, is that structural changes in the industry should be encouraged when they result in improved economic efficiency and serve the broader public interest. *Resolution Re-Affirming NARUC's Fundamental "Principles to Guide the Restructuring of the Electrical Industry*," NARUC Resolution (November 10, 1999)[hereinafter *Principles Resolution*]. This resolution is attached as Appendix B. To accomplish these improvements in the markets and to serve the public interest, many States decided to "deregulate" their electricity markets.

II. CONSUMER PROTECTION ISSUES

The most important goal in the development of retail electric competition plans has been to improve consumer welfare. The move to open markets in the electricity industry was undertaken with the recognition that the outcome must ultimately protect consumers in the respective States. As previously noted, NARUC's members have the obligation under State law to ensure 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 that are just, reasonable and nondiscriminatory for all consumers. *See Hearings*. Thus, consumer protection issues have been at the forefront of NARUC's members' decision-making on retail electricity competition plans.

At its convention in November 1999, NARUC reaffirmed its "Principles to Guide the Restructuring of the Electric Industry." In that resolution, NARUC once again stated that "all consumers must share the benefits of structural improvements and be protected from anti-competitive behavior, undue discrimination, poor service and unfair service practices." Because our member commissions are best suited to ensure that restructuring does not harm consumers, NARUC supports State authority to ensure that retail electric competition does not result in the loss or degradation of service to rural, residential, or low-income consumers. *See, Resolution Adopting "Positions on Issues in Federal Legislation to Restructure the Electric Industry*," NARUC Resolution (March 8, 2000)[hereinafter *Federal Legislation Resolution*], attached as Appendix C. To accomplish this, NARUC has worked to establish guidelines to be utilized in the restructuring debate. Because each State will have unique consumer protection needs, NARUC has urged that Congress should not preclude a State or State commission from prescribing and enforcing consumer protection measures that are more prescriptive than Federal requirements.

In a restructured industry, consumer protections that guard against undue discrimination, failure to meet minimum service quality and safety requirements and other unfair business practices should be preserved. In a competitive environment, consumer abuses such as deceptive marketing practices should also be prevented.

NARUC has researched, debated, and commented on many of the consumer protection issues on which the FTC is gathering data. Some of the more specific consumer protection measures are discussed below. The States and State commissions filing comments with the FTC will provide State specific details on these issues. NARUC's comments reflect efforts undertaken to aid in the development of sound consumer protection policies.

Right to Know and Product Labeling. NARUC believes that one of the outcomes of restructuring the electric industry will be improved and informed customer choice that will in turn lead to more efficient markets, increased resource diversity and improved environmental quality. To further the development of informed customer choice, NARUC supports initiatives leading to minimum, enforceable uniform standards for the form and content of disclosure and labeling that would allow retail and wholesale consumers to easily compare price, price variability, resource mix and environmental characteristics of their electricity purchases. NARUC has urged States adopting retail direct access programs to include such enforceable standards of disclosure and labeling. *See, Resolution in Support of Customer "Right-to-Know" and Product Labeling Standards for the Retail Marketing of Electricity*, November 20, 1996 [hereinafter "*Right-to-Know*" *Resolution*], attached as Appendix D. As the individual State comments will detail, many of the States have actively instituted the foregoing consumer protection principles in their restructuring plans.

To further facilitate "right-to-know" policies, NARUC and other state and federal regulators formed the National Council on Competition and the Electric Industry, which conducted a Consumer Information Disclosure Series. This joint undertaking of State utility regulators and State legislators initiated a major research effort to provide the consumer and policy research needed by States and others to implement programs that could include enforceable standards of disclosure and labeling. *See,* Moskovitz, David, *et al*, *Synthesis Report: A Summary of Research on Information Disclosure*, National Council on Competition and the Electric Industry (1998). Details of this research can be accessed at the Council's website at http://www.ncouncil.org/. The research has led to the development of a model information disclosure policy for implementation by the States, which can also be accessed on the Council's website.

In addition to the development of model information disclosure policy, NARUC has supported efforts to remedy "cramming" and "slamming" on consumers' bills because States are the first line of defense against consumer fraud and abuse. As we have learned in telecommunications and as we are learning in energy restructuring, NARUC's member commissions, along with State attorneys general, are the agencies that consumers call for assistance, that handle complaints, and that must provide necessary remedies against firms that will not comply with legal requirements. States must have the authority to continue to protect consumers against "cramming" and "slamming" abuse. *See, NARUC Response to Chairman Bliley* (May 16, 2000)[hereinafter *Bliley Response*], attached as Appendix E.

Aggregation. Another important tool in the creation of more efficient markets during restructuring is the tool of aggregation. As with other consumer protection measures, States are uniquely qualified to determine how to shape aggregation programs. As consumers explore this option, State authority to determine the terms and conditions of retail service, including the terms and conditions upon which aggregation is available will help consumers purchase power more effectively. Additionally, Congress and the federal agencies should affirm that aggregators are subject to State licensing, registration and consumer protection requirements. *See, Federal Legislation Resolution.*

Affiliate Codes of Conduct, Affiliate Accounting Rules. Protecting consumers in a restructured environment essentially means protecting them from market power, oftentimes exerted through abusive affiliate activities. In 1996, NARUC's Subcommittee on Accounts and the Staff Subcommittee on Strategic Issues formed a Task Force with representatives from the State commissions and the Securities and Exchange Commission (SEC) to investigate what regulatory tools are needed to prevent cross-subsidization as retail electricity markets are restructured. On February 20, 1997, the Task Force issued a draft White Paper titled, "Tools Needed to Prevent Cost Shifting and Cross Subsidies Between Regulated and Non-Regulated Affiliates." The Task Force found that non-structural safeguards may not be sufficient in preventing abuse of market power in strategic markets such as the electric generation market. The safeguards governing the behavior and structure of utility relationships with affiliates and non-regulated divisions operating in energy markets are commonly referred to as "Codes of Conduct." The purposes of Codes of Conduct include: preventing preferential treatment, especially to affiliates; aiding in the development of competitive markets; ensuring that utility ratepayers do not subsidize unregulated utility affiliates; removing the uncertainty for both utilities and their competitors; creating barriers to self-dealing; and addressing how an incumbent utility shall conduct business with an affiliate to promote fair competition and a level playing field among all participants.

At our annual convention in 2000, NARUC passed a resolution that accepted a White Paper entitled "Codes of Conduct Governing Competitive Market Developments in the Energy Industry: An Analysis of Regulatory Actions." *See*, *Resolution Accepting White Paper on Codes of Conduct Governing Competitive Market Developments in the Energy Industry:An Analysis of Regulatory Actions***,** NARUC Resolution (November 15, 2000). The white paper outlines five intentions and purposes of codes of conduct as derived from the research based on various State surveys and the discussions with various stakeholders. Based on this research, the white paper notes that codes of conduct represent a behavioral approach to mitigating market power. Additionally, codes of conduct are used to prevent undue preferential treatment and promote fair competition. Another reason for adopting codes of conduct is to assure the development of an appropriate relationship between incumbent companies and their unregulated affiliates and are often an important tool in the transition to a restructured industry. Codes of conduct also allow for the relevant regulating authority to regulate based on conduct rather than on the legal status of the entity providing service. And finally, codes of conduct are a pro-active approach to addressing the potential abuse of market power. While not binding, many States have looked to this paper for guidance on this issue. A copy of the paper can be accessed at http://www.naruc.org/Resolutions/2000_conv/codes_of_conduct_white_paper.htm.

In addition to the Codes of Conduct White Paper, NARUC approved the "NARUC Guidelines for Cost Allocations and Affiliate Transactions" (Guidelines) addressing electric and gas operations on July 12, 1999. The Guidelines are intended to provide guidance to jurisdictional regulatory authorities and regulated utilities and their affiliates in the development of procedures and recording of transactions for services and products between a regulated entity and affiliates. The prevailing premise of the Guidelines is that allocation methods should not result in subsidization of non-regulated services or products by regulated entities unless authorized by the jurisdictional regulatory authority.

While these comments are not an exhaustive exploration of the questions posed by the FTC in the Consumer Protection section, they do highlight the continuing and intensive efforts by the States and NARUC to develop prudent policies that will ultimately best serve the consumers NARUC's members aim to protect. We anticipate that in their comments, individual State commissions will provide more specific information on their activities in this area.

III. RETAIL SUPPLY ISSUES

In implementing electric restructuring, one of the most critical factors is to ensure that the introduction of retail choice not leave residential and small business customers behind through the lack of adequate retail supply choices. Recently, the National Regulatory Research Institute (NRRI)[1] wrote a report on this issue for NARUC. The report by NRRI outlines the approaches adopted by three States, California, Massachusetts and Pennsylvania, in creating conditions/incentives to ensure a robust retail market. *See, Rose, Kenneth, Electric Restructuring Issues for Residential and Small Business Customers, National Regulatory Research Institute,*

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[1] Established in 1976, the NRRI is the official research arm of NARUC. Though most noted for its research reports and analytic studies, NRRI also provides such services as assistance in commission restructuring, quick response assistance, and educational forums.

June 2000. A copy of this report can be accessed at http://www.nrri.ohio-state.edu/roseken.htm.

According to the report, what has greatly complicated implementation of retail choice is the attempt to reconcile the consequential, but contradictory goals of first, making sure residential and small business customers benefit or are at least not harmed by competition; second, encouraging the development of an efficient and competitive retail market (for example policies aimed at limiting market power); third, having broad customer participation; fourth, protecting incumbent utilities from potential market losses (so-called "stranded costs"); and fifth, maintaining "system benefits" that include system reliability, low-income assistance, and conservation and renewable programs. While every State has addressed, to varying degrees, each of these five overall goals, none has, or is likely to meet, all of them simultaneously.

As the report notes, these goals come into direct conflict when existing customer rates are unbundled into various price components such as a generation price, which has been given various labels such as standard offer, shopping credit, price to compare, backout rate and other labels; customer charges, which include charges for "stranded costs," low-income customer assistance, conservation and renewable programs, and other items; transmission and distribution charges, for the "wires" that remain regulated; and in many States, an automatic discount off the previously regulated rates.

Since States often also establish price ceilings during a transition period, all these price components must fit under the ceiling, which is the beginning of the practical difficulty. If the last three price components are established separately, this may mean that the generation component is set below what a competitive retail market would establish as its price. The result is insufficient "headroom" for competition to occur. As a result, few customers select an alternative supplier, as has occurred in several States, because few competitive options are being made available to them. The experience in the first States to adopt retail access indicates that there is a strong positive correlation between the economic incentive to select a supplier (the generation "price to compare" or standard offer relative to the retail market price) and the percentage of customers that have selected a supplier.

To avoid this problem, some States have established a generation price, or “shopping credit,” that is set sufficiently high so that alternative suppliers are encouraged to enter the market. While this avoids the problem of insufficient “headroom,” at least initially, the method has raised additional issues. First, even with a generation price well above the retail market price, inducing many alternative suppliers to offer customers lower prices, and vigorous customer education to inform customers of their options, many customers remain at the established generation price. Preliminary evidence suggests that these customers may be disproportionately the elderly and low-income households. A second limitation, which is a limitation of any method that sets the generation price in advance without market adjustments, is that while there may be sufficient headroom initially, over time it may be eroded as market conditions change. Suppliers may abandon the area and try to “dump” customers back to the incumbent supplier at the established generation price.

The report notes that there are two general categories of methods used by States to determine the generation price. The first is market-based methods, which include direct wholesale pass through and standard offer auctions. The second is composed of administratively determined methods that base the price on the incumbent utility’s generation costs or a market estimate. While there are advantages and disadvantages to the various methods, market-based methods are better able to reflect market conditions and, if periodic adjustments are made, can change as market prices change over time. Because of the numerous factors that determine a retail price, it is difficult for administrative methods to simulate a dynamic market price, particularly in advance of actual market experience. At best, administrative methods are only rough approximations of the actual market price. Another advantage to market-based approaches is that they spread the benefits of a competitive market to all customers, not just those savvy enough to select a supplier.

The report goes on to detail that because of the design of most transitional unbundling schemes, if upward pressure continues on wholesale prices, residential and small business customers may find themselves in an increasingly disadvantageous bind of higher prices, few or no competitive options, or both. For customers served by an incumbent supplier, the generation "price to compare" may either continue to be below a competitive retail price, so that few competitive options are made available to them, or , when the generation price is sufficiently high to allow competitive suppliers to enter the market initially, the situation does not remain that way as wholesale prices move above the set retail price. In addition to the low (or negative) retail margin, uncertain and unstable prices increase the risk for alternative suppliers and force them to charge higher prices, abandon retail markets, or never enter in the first place. There will be little complaint from the incumbent supplier about the generation price, at least during the transition period, since its total generation compensation also includes the payment for "stranded costs." Also, the incumbent supplier or its affiliate is able to maintain a dominant market share. When the incumbent utility has exited the generation business either mostly or entirely, upward pressure is placed on the generation price since it is now supplied by the new owner or owners of the existing generation resources or is purchased in the wholesale market. However, since the amount of the "stranded cost" payment was determined when lower prices were expected (either estimated or determined by generation asset sales), customers continue to pay for "stranded costs" that never materialize. The combined result is a higher price of generation and continued payment for "stranded costs" to the former owner of the generation assets.

The report points out that perhaps one of the most significant issues facing small customers is the possible impact of market power and price discrimination. Due to customer demand characteristics, relatively concentrated retail markets, and generation and transmission constraints that limit retail customer access to alternative suppliers, there may be significant opportunity for suppliers to exploit market power and raise their price above what a competitive market outcome would be. Also, since suppliers will be able to segment groups of customers, the opportunity and incentive exists to charge a higher price to smaller customers and sustain the higher price for an appreciable period of time.

Finally, the report concludes that over time, as transition periods end, more new generation will enter the market, and transmission constraints will ease, causing prices to moderate and all customers to benefit. However, some transition periods run until the end of this decade and, at this time, it remains to be seen to what extent supplier market power, both wholesale and retail, will develop to obstruct or prevent the full development of a competitive generation market. At this critical stage of restructuring, the report recommends that States need to seriously consider policies that encourage the development of a competitive generation market and ensure the spread of the benefits to as many residential and small business customers as possible. NARUC has consistently supported this recommendation.

IV. RETAIL PRICING ISSUES

NARUC has recognized that competitive markets have the potential to reduce the total costs of electricity production in the country, to lower rates if benefits accrue to customers fairly, and to stimulate innovation and new investment. *See, Principles Resolution*. It is important, however, that policy-makers should recognize that, in certain instances, barriers to efficient competition prevent market participants from correctly valuing the full costs and benefits of certain production and consumption decisions. Many aspects of utility regulation, and many utility practices, including integrated resource planning, have been developed to address these market barriers, and have delivered significant benefits to consumers and the nation. Some of these benefits include energy efficiency, renewable resource technologies, low-income energy assistance programs and research and development funds.

For public policy reasons and because not all potential risks will be fully reflected in short-term market prices, it will be necessary for policy-makers to promote and implement mechanisms that will serve the long-term needs and aspirations of the nation. *See Principles Resolution*. To the extent that cost-effective investments in energy efficiency, renewable resources, and research and development are not fully valued in the competitive marketplace, there will continue to be a need for alternative methods for capturing the benefits that they offer.

To that end, NARUC has encouraged the incorporation of public benefits in restructuring initiatives. In 1994, NARUC first noted that 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. *See, Resolution on Public Benefits*, NARUC Resolution (July 26, 2000), attached as Appendix G. Last year, NARUC reaffirmed its commitment to its insistence that Public Benefits must be included in any electric industry restructuring legislation. *See id*. Our members also resolved to that further study of societal costs and benefits is warranted prior to NARUC supporting any particular implementation or funding mechanism for the continued support of Public Benefit Programs. *Id*. To assess the development of public benefits programs, the National Regulatory Research Institute in conjunction with the American Council for an Energy Efficient Economy (ACE3) conducted an extensive survey on the public benefits programs in the various States. An initial report based on responses from approximately 38 States was presented to NARUC members at the 2001 Winter Meetings. The report can be accessed at NARUC's website at www.NARUC.org. NRRI is continuing this research into State public benefit programs. That survey can be accessed at http://www.aceee.org/briefs/mktabl.htm.

For a more thorough analysis of this issue, many of the States will be filing comments detailing their respective policies with regard to the questions posed in this section of the Notice.

V. MARKET STRUCTURE ISSUES

As State and Federal policymakers explore solutions to the challenges before us, a major obstacle that the energy industry faces is unpredictability and uncertainty. When the right economic or market signals are sent there is an appropriate corresponding response by the market participants. If the market participants perceive that the rules are constantly changing affecting the ability of the market to stabilize, the participants will be reluctant to invest in development of the market. NARUC has supported clear policies on market structure issues and outlines some of those efforts in the following:

Jurisdiction. Given the complex nature of developing competitive retail electric plans and the structure of the markets in those plans, NARUC has been working internally and through litigation to examine the link between retail transmission jurisdiction and the ease of retail access. We anticipate that recommendations on this issue could be issued later this year.

Through litigation, NARUC and its members have been working to clarify some of these jurisdictional issues. On February 26, 2001, the U.S. Supreme Court granted *certiorari* in New

York, *et al*. v. FERC (00-0568) and in Enron Power Marketing, Inc. v. FERC (00-0809). Both petitions had sought review, on different grounds, of a June 30, 2000, ruling by the D.C. Circuit Court of Appeals upholding FERC Order 888. Order 888, required all utilities under FERC jurisdiction who own, operate, or control wholesale transmission facilities to file nondiscriminatory open-access transmission tariffs offering services to third parties comparable to the utilities' own uses of their transmission facilities. The order presented a single *pro forma* open-access transmission tariff (OATT) describing the minimum terms and conditions of the services that transmitting utilities must provide to others. In so doing, FERC envisioned increasing competition amongst power suppliers through increased access to the transmission grid and giving individual customers increased choices in choosing their electricity providers. In issuing this Order, FERC asserted jurisdiction over retail transactions when states unbundled retail rates into charges for delivery and electricity, decided that it would set the rates that a seller of unbundled wholesale energy would pay for the use of local distribution facilities, and preempted the States' rate treatment of stranded costs. Oral arguments will be heard during the Court's 2001-02 term sometime after October 1, 2001.

In its *Federal Legislation Resolution*, NARUC outlined why it is important that the Supreme Court, the Congress, FERC and the FTC support State authority to regulate retail transmission services. Because they have the obligation to ensure the just, reasonable, and nondiscriminatory electricity service for all consumers, State regulators should have the jurisdictional authority to regulate services supplied to native load customers. Moreover, State commissions are in the best position to take local conditions into account as they fashion policies to govern transmission investment, siting and cost recovery and allocation issues.

Market Power. As competition in retail power supply markets evolves, after-the-fact antitrust enforcement might not be sufficient to protect against market power abuses in the transition from monopoly to competitive markets. NARUC believes that abuse of market power can reduce the economic gains to consumers from a restructured electric power industry. *Resolution Relating to Market Power in a Restructured Electric Power Industry*, NARUC Resolution (July 29, 1998), attached as Appendix H. Our resolution noted that abuse of market power can be addressed by various governmental actions, ranging from behavioral rules and functional unbundling to structural separation and divestiture, with varying effects on consumers and firms.

Noting these concerns, NARUC resolved that Congress should not preempt jurisdiction in the States to address market power concerns; and State legislatures should give clear and adequate authority to the State commissions to protect all classes of consumers from the abuse of market power, including the authority to require behavioral and structural remedies to address excessive market power. Further, any market-power remedies should balance the benefits and costs, including reliability impacts and economies of scale and scope, from the perspective of all classes of electricity consumers.

NARUC believes a continuum of options for the mitigation of market power should be available, and has urged State legislatures and Congress, in considering restructuring, to preserve State flexibility to use these options as needed. Any policy developed on this issue should clarify the authority to use accounting conventions and codes of conduct, which may be sufficient safeguards in some cases, as noted previously in the section on affiliate conduct. The policy 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. Additionally, any policy should clarify that States have clear authority to require the formation of appropriate State and regional institutions where necessary to support competitive electricity markets. As market power abuse may ultimately require the application of structural remedies, policies should clarify that the States are authorized to require divestiture where appropriate and necessary.

In order to mitigate market power abuse the U.S. Department of Justice, the FTC, State attorneys general, and FERC must cooperate to monitor, prevent, and correct excessive market power in the electric power industry, with attention to market concentration, entry barriers, collusion, and other anti-competitive activities.

Reliability. In structuring electricity markets, maintaining the reliability of the nation's electric system is one of the most critical issues. We share the growing concerns of many observers that reliability of the nation's electric power system will suffer as wholesale generation and transmission markets evolve. NARUC strongly believes that the States must have the authority and the flexibility to create regional mechanisms such as inter-state compacts and regional reliability boards, for the purpose of addressing transmission reliability issues. As noted, the States must also have the appropriate tools, information, and authority to address market power so as to ensure the safe, reliable and reasonable access to electricity.

To this end, NARUC has been actively involved in the development of mechanisms and polices to maintain reliability. NARUC has been working with Congress and the various stakeholders to develop and recommend appropriate federal policies to strengthen the reliability of the North American bulk power system. However, these problems cannot be solved only at the wholesale level. Accordingly, individual States are working with their electric utilities and with each other on a regional basis, to complement the efforts of FERC, the North American Reliability Electric Reliability Council (NERC), and regional reliability councils aimed at strengthening the safety, security and adequacy of our electricity infrastructure. For example, the West has a history of grid cooperation between industry participants and the Committee on Regional Electric Power Cooperation (CREPC). The New England region and New York have been utilizing the Northeast Power Coordinating Council to enhance the reliability in that region.

NARUC has adopted guiding principles intended to strengthen reliability. *See, Federal Legislation Resolution.* We support legislation establishing mandatory compliance with industry-developed reliability standards and providing explicit authority to FERC and the States to cooperate to enforce those standards. We also support the inclusion in any federal proposal of workable mechanisms to support energy efficiency programs that enhance reliability. However, NARUC **cannot** support reliability legislation that fails to provide a continuing role for States in ensuring reliability of all aspects of electrical service, including generation, transmission, and power delivery services or results in FERC preemption of State authority to ensure safe and reliable service to retail consumers.

Regional Transmission Organizations (RTOs). Recognizing the critical regional implications of system reliability, NARUC's reliability policy includes a regional advisory role for the States. We also believe that voluntary regional mechanisms can be fashioned to support FERC's RTO Rule, Order No. 2000. *See, Bliley Response*. Working with FERC individually or regionally, States can help assure independent grid operations as part of the process of implementing Order No. 2000. In order that State expertise be utilized, States should be able to address ongoing concerns in RTO functions after the initial RTO development period, including reliability, market monitoring, pricing, congestion management, planning and interregional coordination.

NARUC believes that it is possible for efficient and effective RTOs to focus on wholesale transmission services notwithstanding State jurisdiction at the retail level.[2] The benefit of preserving a State role is to enable State commissions to take local needs into account. Moreover, as Order No. 2000 is implemented, we expect that regionalism will continue to grow in importance. Accordingly, NARUC strongly supports the parallel development of cooperative regional regulatory mechanisms to support non-discriminatory, open-access transmission services. *See, Bliley Response*.

VI. OTHER ISSUES

Demand Side Management. NARUC and its members recognize that competitive energy providers will offer their customers products which reflect prices available in the wholesale markets. When supplies are constrained, markets will be most efficient where customers are able to react to prices, thereby providing long-term benefits by mitigating market power, furthering innovation, easing transmission and distribution constraints, increasing diversity, encouraging reductions in unnecessarily costly energy usage, and improving reliability. Cognizant of these conditions, NARUC adopted a resolution in July 2000, urging that when remedying situations of inadequate supply or constrained transmission, demand responses to market prices should be equally and fairly compared to alternatives which require the

[2] The Florida Public Service Commission (FPSC) noted in its comments to the FTC, FERC unfortunately denied a request by the FPSC to have a technical conference on the roles the FPSC and the FERC would play in the GridFlorida RTO. (Letter from Cynthia B. Miller, Bureau of Intergovernmental Liaison, State of Florida Public Service Commission to the FTC.)

construction of new transmission or generation. *Resolution Regarding Equal Consideration Of Demand and Supply Responses in Electric Markets***,** NARUC Resolution (July 26, 2000) attached as Appendix I. To that end, NARUC has supported research initiatives into demand side management by the Regulatory Assistance Project. Information on these research initiatives can be accessed at our website at http://www.naruc.org/Committees/ere/Publications.htm.

Distributed Generation. NARUC recognizes that advances in smaller-scale generation options have played a significant role in the move to restructure electricity markets. NARUC supports Congress requiring the establishment of national interconnection and power quality standards, developed and adopted by appropriate technical standards organizations, such as the Institute of Electrical and Electronics Engineers, Inc. for facilities by a date certain. *See, Federal Legislation Resolution*; *see also, Resolution Regarding Interconnection Standards for Small-Scale Generating Facilities*, NARUC Resolution (July 1998), attached as Appendix J. Additionally, NARUC believes that the States should have the flexibility to adapt these rules through their own rulemaking procedures.

In addition, NARUC supports removing barriers to State implementation of interconnection or to net metering. Accordingly NARUC is pleased with FERC's recent ruling that neither the Public Utility Regulatory Policies Act of 1978 (PURPA) nor the Federal Power Act (FPA) stand as an obstacle to net metering. On March 28, 2001, FERC issued an order denying MidAmerican Energy Company's request to overturn the Iowa Utility Board's (IUB) order establishing net metering/billing. That order called for utilities to interconnect with qualifying Alternative Energy Production facilities (AEP) with a single meter which monitors only the net amount of electricity sold or purchased from the utility on a monthly basis. FERC found that the State regulation of net metering was not preempted by federal law because not every flow of power constitutes a sale invoking the requirements of federal law.

Additionally, NARUC sponsored a paper by the Regulatory Assistance Project entitled, "Profits and Progress Through Distributed Resources." That paper can be found on our website at http://www.naruc.org/Committees/ere/Publications.htm. This paper states that, "along with better known and proven energy efficiency and load management technologies, … distributed [generation] resources are poised to revolutionize the electric utility industry." The paper goes on to note that "distributed [generation] resources can provide a very wide range of benefits depending on the type of resource deployed, where it is installed, and when and how it is operated." Because of these benefits, distributed generation will play a key role in enhancing reliability and meeting demand. For example, distributed generation can provide "spinning reserve, black start capability (micro turbines can go from cold start to full load in two minutes), load following, and reactive power." Additionally, in terms of reliability, "increased distributed [generation] resource use can lead to shorter and less extensive [power] outages. The small size of distributed resources means the same level of reliability can be achieved with lower installed generation." Finally, well-planned distributed generation reduces transmission and distribution load constraints and will thus continue to play a role in easing these problems.

NARUC recognizes that distributed generation offers significant advantages in meeting specific customer needs, reducing environmental impacts, meeting congestion and reliability needs, and avoiding additional transmission expansion and expenditures.

CONCLUSION

NARUC looks forward to continuing to work with the FTC and other federal agencies on the complicated and evolving nature of developing retail electricity competition policies. While the comments above are not exhaustive of each and every State's unique approach to the various issues highlighted in the Notice, the State commissions and legislatures -- which are the entities best suited to address these issues -- are acting with great care and precision to ensure the continued reliability of electric services and universal access to retail services and public benefits previously provided by a vertically integrated industry.

Respectfully Submitted,

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APPENDIX A

Testimony of Commissioner William H. Nugent
Before the
Senate and Energy Natural Resources Committee
March 21, 2001

Mr. Chairman and Members of the Committee:

Good morning. My name is Bill Nugent. I am a Commissioner on the Maine Public Utilities Commission and First Vice President of the National Association of Regulatory Utility Commissioners, commonly known as NARUC. I greatly appreciate the opportunity to appear before the Senate Energy and Natural Resources Committee on behalf of NARUC and 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. Its membership includes the state public utility commissions for all states and territories. NARUC's mission is to serve the public interest by improving the quality and effectiveness of public utility regulation. NARUC's members regulate the retail rates and services of electric, gas, water and telephone utilities. We have the obligation under State law to ensure 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 that are just, reasonable and nondiscriminatory for all consumers.

NARUC's membership has been and continues to be central to the development and implementation of policy initiatives affecting the nation's energy industry and its consumers. For better or worse, the States are the proving grounds for innovations in energy policy. One observation that can be made regarding State energy policy activities is that one size does **<u>not</u>** fit all. States and their energy industry stakeholders are experimenting with many different solutions to the energy challenges that are confronting this Nation. These proposals range from retail competition implementation to demand side and renewable energy incentives to the use of new technology applications. Clearly, in light of the difficulties being experienced not only in the Western region, additional solutions are necessary.

As policy makers we all must be cognizant of the fact that, as we explore solutions to the challenges before us, the main obstacle that the energy industry faces is a paucity of predictability and certainty. When the right economic or market signals are sent there is an appropriate corresponding response by the market participants. If the market participants perceive that the rules are constantly changing and therefore the market will never develop or mature, the participants will not invest in development of the market or the production mechanisms to participate in that market.

Historical Perspective

As the electric power industry developed the technical generation and transmission capability in the early part of this century, the industry was transformed from a local and urban industry into one capable of producing large amounts of power at a central location and transmitting this power vast distances. As efficiencies improved prices declined. For most of the twentieth century States have regulated all aspects of bundled retail electric service and rates.

The inability of the States to regulate prices and other aspects of electricity sold in interstate commerce under the Constitution and the absence of Federal regulation of those activities created a vacuum of regulation over electricity flowing in interstate commerce. The enactment of the Federal Power Act in 1935 constituted the first comprehensive effort to bring interstate aspects of the electrical power industry under governmental regulation.

As a consequence of major power outages during the late 1960's-early 1970's and the energy crisis of the 1970's, Congress held extensive hearings looking into specific electricity blackouts and capacity shortages. Much of this attention focused on the matter of interconnection of utilities as a method of assuring greater reliability and coordination among utilities. Out of these congressional reviews, more formalized planning responsibilities and wheeling requirements were incorporated into the Public Utility Regulatory Policies Act of 1978 (PURPA).

PURPA provided that State public utility commissions should consider and determine whether to adopt cost-of-service and other standards that were contained in PURPA section 111 and 113. Section 201 and 210 of PURPA provided that certain qualified facilities (QFs) could sell their power to their host utility at that utility's State-determined avoided cost. There are two categories of QFs: cogeneration facilities, and renewable facilities. The Federal Energy Regulatory Commission promulgated general rules in 1980 on avoided cost calculations, and by 1982 all the State commissions had developed specific formulas and methods to administratively-determine and implement avoid costs. One State early on, New Jersey, set its avoided costs at the Pennsylvania-New Jersey-Maryland (PJM) wholesale market rate.

While other PURPA provisions purported to encourage wheeling of electricity, they were for the most part ineffective. Wheeling of electricity took place only voluntarily. Wholesale electricity markets were limited, except where State commissions encouraged and utilities formed tight power pools, such as PJM and the New England Power Pool (NEPOOL). To break down the barriers to a more robust wholesale power market, Congress enacted Title VII of the Energy Policy Act of 1992 (EPACT).

EPACT provided that FERC could mandate wheeling of electricity. This provided generators with open transmission access to any wholesale buyer of electricity. EPACT also created Exempt Wholesale Generators (EWGs). These EWGs could, subject to State siting and environmental review, build power plants to sell electricity on the wholesale markets.

By 1994, the wholesale price of electricity fell dramatically because of the surplus of generation capacity. Large industrial customers in high cost States asked their State legislatures or State commissions to allow retail customers to have direct access to wholesale markets. Today, 25 States, plus the District of Columbia, are in the process of implementing retail competition laws and/or regulations. These States have also provided for recovery of stranded costs. Most of these States have also either allowed or required their host utilities to divest themselves of their generation capacity, in order to break up vertical market power.

Independent System Operators (ISOs) were set up in PJM, California, and New England to coordinated regional wholesale markets. After the initial success of these ISOs, FERC required all jurisdictional utilities to organize themselves into Regional Transmission Organizations (RTO) in FERC Order 2000. These RTOs will help to coordinate regional transmission systems and regional power markets. They are also intended to monitor regional markets and plan regional transmission expansion.

State commissions must have a greater role in RTO governance and oversight than is now provided by FERC Order 2000. In particular, State commissions are the entities most directly concerned with monitoring local and regional markets because <u>retail</u> customers are most affected by market power abuses. In addition, the State commissions typically are the entities that must coordinate and approve transmission expansion and siting consistent with regional plans. State commissions have consistently expressed a willingness to work with FERC on such regional issues, but thus far the FERC has taken a position that it can and should preempt the field. Congress should provide an appropriate State role for regional oversight of RTOs concerning market power monitoring and transmission expansion planning, and for other areas where State commissions in a given region can cooperate and have the distinct advantage of knowledge of the region and the workings of its energy industries.

On the gas side, in 1977 the nation had just suffered through natural gas shortages and curtailments that were caused by an imbalance of supply and demand in the interstate gas market. This supply-demand imbalance can be traced to the 1954 *Philips* Supreme Court decision, which interpreted the Natural Gas Act of 1938 to extend federal authority to regulate the wellhead gas price of gas sold in interstate commerce.

Congress, as part of the Energy Policy Act of 1978, enacted the Natural Gas Policy Act of 1978 (NGPA) and the Fuel Use Act (FUA). The NGPA provided for phased deregulation of wellhead gas. By 1985, the wellhead price of natural gas was effectively deregulated. The FUA provided that there would be no new gas-fired electric generation after 1978. However in 1985 the FUA was repealed. Thus, for seven years there was a federally mandated moratorium on new gas-fired electric generation.

As the phase-in for deregulation ended, wellhead prices dropped because the supply of gas was more than adequate for the demand and higher-cost gas wells were shut down. To encourage further gas consumption, the FERC issued FERC Order 436 (in 1985) and Order 500 (in 1987). Specifically, with these two orders, the FERC provided for voluntary open access to gas pipeline transportation, coupled with offering take-or-pay gas wellhead contract relief for high cost gas. This was the equivalent of allowing for a stranded cost recovery. It is worth noting that end use gas customers only paid about 11 cents for each dollar of take-or-pay relief, contrasted with the $1 for $1 stranded cost recovery for electric utilities in FERC Order 888.

During this period, gas supplies remained abundant when compared to gas demand; this was reflected in the continued low wellhead price of natural gas. In 1992, the FERC issued Order 636, which mandated unbundling of gas as a commodity for the transportation service provided by interstate pipelines. Order 636 also provided for pipeline capacity release and a secondary market for released pipeline capacity. In FERC Order 637, issued in 2000, FERC removed the rate cap on short-term secondary pipeline capacity. This resulted in the development of a spot market for natural gas, a secondary market for capacity, ancillary gas services (such as storage), and 40 gas transportation hubs that are market centers for gas.

Since the late 1980s, nearly all State commissions have allowed large industrial and commercial customers to have unbundled gas service, through which they can purchase gas transportation from their distribution company and directly purchase wellhead gas. Currently (either as a pilot program or part of a broader customer choice program), 23 states and the District of Columbia now allow retail residential customers to purchase gas directly from the wellhead (typically through aggregators or marketers).

Energy Trends and Markets

The following observations are not listed in any particular order because many build upon each other; they should be considered as a whole, not separately. While these trends do not provide us easy answers to our Nation's energy policy challenges, but these observations may help to identify the problems that we must soon confront.

Natural Gas Trends

Trend 1 – Gas demand has increased, production has not kept pace, and there is no "quick fix"

Natural gas wellhead prices more than doubled for the fourth quarter of 2000 compared to the fourth quarter of 1999, and working gas storage was down in 2000 compared to 1999. Additionally, from 1994 through 1997 while the growth in domestic gas reserves exceeded incremental gas production, domestic gas production was projected to increase by only .05 percent in 2000 compared to 1999 (from 18.66 to 18.76 Tcf). At the same time, nearly all-new electricity generation being is gas-fired. Therefore, a principal reason for the increased gas prices is the increased demand for gas caused by new gas-fired electric generation (gas peaking turbines and combined-cycle gas turbines). Domestic gas production is likely to increase in response to higher gas prices, but in the short and mid-term most of the increased supply is likely to come from existing gas fields in Canada. While it might take only six months to explore and drill a gas well, it takes years to build a pipeline to transport it, if the gas does not come from existing or nearby existing gas sources which have pipelines in place.

These trends are well illustrated in Maine. In 1997 the closure of the Maine Yankee Nuclear Generating Station reduced Maine's electric generating capacity from 3,100 megawatts (mW) to 2,200 mW. Over the last three years we have added more than 1,600 mW of new, gas-fired generation, bringing our total to 3,800 mW, more than double Maine's peak demand.

This was made possible by the construction in 1999 and 2000 of two new gas pipelines, the Portland Natural Gas Transmission System, which brings western Canadian natural gas through Maine to the New England Market, and the Maritimes and Northeast Pipeline, which transports gas from the Sable Islands gas fields, 150 miles off the coast of Nova Scotia. These pipes were planned, sited, and permitted before today's higher natural gas prices. There is reason to believe that, in response to today's market opportunities, M&NE will boost its capacity by more than 50 percent through higher compression. And further increases in production off the Canadian Maritimes may be in the offing.

Trend 2 - Convergence

In 1998, over $30 billion in convergence mergers transpired as electric utilities merged with gas pipelines, gas providers, and local gas utilities. These mergers provide the converged companies an opportunity to vertically integrate and also to market BTUs in the form of natural gas or electricity, whichever is more lucrative. This allows the energy industry stakeholders to respond to market demand and preference, while providing them an opportunity to hedge against the uncertainty confronting this industry today.

Trend 3 – Though the majority of natural gas is still being bought on the spot market, market participants are increasing their use of risk management tools

Retail gas customer choice programs have been established in nearly half of the states, but nearly 60 percent of the natural gas consumed is still being bought on the spot market. Without hedging, forwards, or futures contracts, most retail customer prices will continue to be volatile – placing a heavy burden on many small customers. However, in response to this winter's price increases, gas companies and their affiliates, as well as gas marketers, are increasingly emphasizing hedging and other risk management tools.

Trend 4 – States have increased their assistance to residential ratepayers

Nationwide, as a result of increased gas prices, State commissions have redoubled their efforts to inform consumers of the likelihood of increased prices and ways they can lower their gas bills through more efficient usage. State commissions have also been re-examining their disconnection policies for gas customers, provided information on the availability of levelized or budget billing, and energy weatherization and conservation programs. State commissions have also informed customers of low-income energy assistance programs and in many instances have expanded those programs.

Electricity Trends

Trend 1 – Customers are demanding increased reliability

Recently there have been an increased number of major utility interruptions as a result of a lack of generation capacity or the result of problems with equipment failures at the distribution system. Because of our increasing reliance on electro-technologies, including the manufacture of solid state electronic silicon chips, there is an increasing customer desire for fewer electricity interruptions and for higher quality of power, that is, power without voltage sags, surges, spikes, interruptions, or harmonics. Internet farms and informational services are particularly sensitive to power disruptions. As our economy increasingly depends on technologies driven by electricity, reliability becomes exceedingly important to our economic health.

Trend 2 – Reserve Margins

Reserve margins are low in several regions in the country. They are particularly low in California, where utilities are projected to not have enough capacity to serve their customers at times if this summer is average or warmer than normal. And at least according to one major electricity marketer (Dynegy), most regions of the country (the sole exceptions are Texas and New England) will be in a capacity deficit situation through next year.

Trend 3 – Gas fired generation

During 1999, about 80 percent (11,073 mW of the 13,763 mW) of new capacity additions by utilities and non-utilities were gas-fired. Gas-fired units drew heavily on gas supplies during the summer of 2000, the season when a time gas utilities and pipelines traditionally put natural gas in storage. This led to higher gas prices during the summer, lower inventories last fall, and even higher gas prices this winter. While gas prices have since moderated somewhat, this pattern is likely to repeat itself until increased gas supplies reach the market. While it might take as little as six months for gas production to increase, if new gas supplies are located such that additional pipeline capacity is needed, the period for new gas supplies to reach the market could be two years or more.

Nearly all of the additions of generation capacity that are planned for 2000 through 2004 are gas-fired electric generation. Of the 44,410 MW of planned generation capacity, 41,339 (93 percent) are gas-fired. This additional planned electricity capacity, if completed, will provide upward pressure on natural gas prices. If the capacity fails to come on-line as scheduled, most electric reliability regions throughout the country will face electricity capacity shortages, if not immediately, then within the next few years. While it only takes two years for a gas-fired plant to be built once sited, it takes coal plants several years. Petroleum-fired plants also have high fuel prices, and currently no nuclear plants are planned. New hydro capacity is limited; and the amount of capacity from waste heat (cogeneration) and renewables is also limited.

Trend 4 – Generation jurisdiction shift from State to FERC

During 1999, three quarters (10,266 mW of the 13,763 mW) of new capacity added was added by non-utilities. Most of this capacity is being sold on regional wholesale electricity markets, which are regulated by the Federal Energy Regulatory Commission (FERC). As State commissions allow retail electricity competition, they often also allow or require generation plant divestiture by the host utility. Most of these generation assets are acquired by non-utilities and the power is sold on regional wholesale markets, regulated by FERC.

This is, I believe, the right model. But it requires a clear vision on the part of the FERC, consideration of the facts on the ground in each of the different regions of the country, and prompt decisions by the Commission. Delay costs ratepayers—the people you and we serve—a great deal of money. At stake right now before the FERC in a current controversy over installed capability is $90 million for Maine ratepayers alone, and perhaps ten times that amount across the six New England states.

<u>Trend 5 – Competitive markets require States to have access to more information not less</u>

State public utility commissions around the country, but particularly in the West, increasingly are faced with refusals by utilities and non-utilities that own generation facilities to provide data. Without requested data, State regulators are severely hampered in their efforts to determine whether there is gaming of the market, through bids that are many multiples of production costs, by withholding of capacity at or near peak, or withholding of available transmission capacity. State commissions need to know which <u>**units**</u> (not plants) are down and/or at what output in megawatts are all units producing. This information needs to be given in a timely manner as a useful average.

Additionally, the Energy Information Administration of the U.S. Department of Energy is proposing to aggregate its data form reports and to withhold data that might be confidential. Without such data, State commissions, State attorneys general, and the FERC will be unable to monitor the markets to ensure the market is free of market power, and that market rates are just and reasonable.

<u>Trend 6 – Nuclear plants are being re-licensed</u>

Ten years ago it seemed certain to many that the operating nuclear plants in this country would be shut down rather than renew their licenses. But today, two have been renewed, additional license renewals are pending, and generating companies are purchasing nuclear units that could not be given away in the late 1980's and early 1990's. Increasingly, nuclear units are seen as a cost effective way to produce electricity in a competitive electricity market. This trend can continue only if the Federal government meets it's statutory obligation to begin excepting spent fuel for disposal and if the Congress appropriates the necessary monies that America's ratepayers have already paid into the U.S. Treasury for the purpose of building a nuclear waste disposal facility.

In conclusion I would like to leave you with one last trend that I will call a "general energy trend," which I believe is accurate regardless of the energy source. Demand for energy is at an all time high and, if current estimates are accurate, each year this demand will continue to increase. Prices for energy have followed suit and increased as well. This trend has placed a severe financial burden on many consumers across the nation.

NARUC believes that the impact of the current energy price increases can be mitigated, in a number of ways. First, for our most vulnerable citizens, Congress should provide substantial increases in funding for the Low Income Home Energy Assistance Program (LIHEAP). We believe that LIHEAP should receive a "core" appropriation of at least $3.4 billion as is proposed in Senator Bingaman's bill (S. 352) plus emergency contingency funding of at least $1 billion as is proposed in Chairman Murkowski's legislation (S. 388 and S. 389).

Second, Congress needs to take action to promote development and encourage the production of renewable energy sources and technologies. Congress must also balance supply/production policies targeted at conventional energy sources (nuclear, coal, gas, oil and hydroelectric) with meaningful incentives and policy to encourage demand reduction and conservation.

Thank you for your attention and availing me the opportunity to testify today. I look forward to your questions.

APPENDIX B

Resolution Re-Affirming NARUC's Fundamental "Principles to Guide the Restructuring of the Electric Industry"

WHEREAS, The issues involved in the restructuring of the American electric industry are of vital importance to the citizens of our nation and are under active consideration in pending Federal legislation; and

WHEREAS, The National Association of Regulatory Utility Commissioners, (NARUC) has consistently recommended certain "Principles to Guide the Restructuring of the Electric Industry" as originally adopted on July 25, 1996, and incorporated in numerous subsequent resolutions, to ensure that this restructuring best serves energy consumers, energy providers, our national economy, and the public good; and

WHEREAS, NARUC has most recently set forth those principles in testimony presented to the United States Congress on October 5, 1999; and

WHEREAS, A re-affirmation of the most fundamental elements of those principles may be of assistance to the United States Congress in its consideration of potential legislation; *now, therefore, be it*

RESOLVED, That the National Association of Regulatory Utility Commissioners, assembled at its 111th Annual Convention in San Antonio, Texas, hereby re-affirms its recommendation that the Federal Congress be guided by the following fundamental principles as it considers policies to govern the organization and operation of America's electric utility industry:

- 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 that 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.

Sponsored by the Committees on Electricity and Energy Resources.
Recommended by the Board of Directors.
Adopted in Convention November 10, 1999.

APPENDIX C

Resolution Adopting
"Positions on Issues in Federal Legislation to Restructure the Electric Industry"

WHEREAS, Congress is in the process of developing legislation to restructure the electric industry; and

WHEREAS, The National Association of Regulatory Utility Commissioners (NARUC) established an Ad Hoc Committee on Electric Industry Restructuring and has been working with Congress and the various stakeholders to discuss and recommend appropriate federal policy with respect to restructuring; and

WHEREAS, The Ad Hoc Committee, through a number of conference calls and meetings has developed positions on some of the various issues that have been addressed in discussions and in pending legislation; and

WHEREAS, The NARUC will continue to develop its positions as the debate on electric industry restructuring moves forward; and

WHEREAS, It is now appropriate that the National Association of Regulatory Utility Commissioners (NARUC), as the national representative of the State regulatory commissions, outline its positions on the issues important in ensuring that legislation serves the interests of consumers, providers, the national economy and the public good; *now therefore be it*

RESOLVED, That the Board of Directors of the National Association of Regulatory Utility Commissioners (NARUC), convened at its March 2000 Winter Meeting in Washington D.C., hereby adopts the attached "Positions on Issues in Federal Legislation to Restructure the Electric Industry" and urges that Congress be guided by these positions as they develop new policies to govern the regulation, organization and operation of the electric utility industry.

Sponsored by the Ad Hoc Committee on Electric Industry Restructuring
Adopted by the NARUC Board of Directors March 8, 2000

Positions on Issues in Federal Legislation to Restructure the Electric Industry

1. **"Grandfathering"**

- NARUC supports grandfathering the legislative and regulatory actions of those States that have elected to implement certain initiatives regarding retail competition. States should continue to have the authority to respond to the unique circumstances under their jurisdiction with regard to restructuring. NARUC also strongly supports the absence of a date certain mandate for States to enact restructuring.

2. **Reciprocity**

- NARUC opposes any provisions prohibiting utilities in non-retail access States from making sales in retail access States.
- Reciprocity requirements are contrary to the very purposes of retail access, which are to create an open market to allow consumers the widest possible choice. Reciprocity limits the number of competitors that are available to lower prices and improve services.
- Reciprocity requirements would tend to force States that have not yet elected to open up their retail markets to do so. This policy is inconsistent with NARUC's previously stated position that States should continue to have the authority to respond to the unique circumstances under their jurisdiction with regard to restructuring.
- Reciprocity provision will result in increased confusion as to entities to whom the prohibition would apply. For example, when providers of electricity serve consumers in more than one State, some of which have

retail access and some which do not, questions arise as to whether a company would be allowed to offer service in a State with full retail access.

- A reciprocity provision would impede interstate commerce, raising constitutional issues.

3. **Interstate Compacts**

- NARUC supports voluntary regional bodies to address siting of transmission facilities.
- Congress should provide an explicit grant of authority to the States and FERC to act in cooperation.
- States should be primarily responsible for forming these entities with only limited intervention from FERC.
- Congress should affirm that States have the primary authority to set up, operate and govern these voluntary regional siting bodies, and FERC would act as an appropriate "backstop" authority where States or regions fail to act.

4. **Reliability**

- 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
- NARUC **cannot** support reliability legislation that fails to provide a continuing role for States in ensuring reliability of all aspects of electrical service, including generation, transmission, and power delivery services or results in FERC preemption of State authority to ensure safe and reliable service to retail consumers.
- Congress should expressly include in legislation: (1) a savings clause to protect existing State authority to ensure reliable transmission service, and (2) a regional advisory role for the States
- NARUC is concerned that a savings clause limited only to "local distribution" could actually be harmful to consumers since it: (1) creates confusion over the responsibility to review service disruptions; (2) implicitly supports the view that legislation preempts State regulation of nondistribution related reliability; and (3) raises the question that NERC (a non-governmental entity) might otherwise cover distribution issues

5. Mergers

- NARUC supports a merger policy where both Federal and State regulators thoroughly evaluate mergers to assess their impact on competition, access to transmission facilities and electric rates.
- NARUC supports merger policy that recognizes State authority to assess retail impacts.
- Congress should enable FERC to extend any statutory review period for good cause.
- NARUC believes that Congress should require prior FERC approval for mergers and acquisitions involving utilities or utility holding companies

6. **Market Power**

- Congress should not preempt jurisdiction in the States to address market power concerns, including the authority to require behavioral and structural remedies to address excessive market power.
- NARUC advocates a continuum of options, such as accounting conventions and codes of conduct, for the mitigation of market power, and urges Congress to preserve State flexibility to use these options as needed.
- 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 authority to require the formation of appropriate State, territory, 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 authorized to require divestiture where appropriate and necessary.
- Congress should also clarify that State regulators have authority to ensure effective retail markets and should eliminate any barriers to the exercise of that authority by the States.

7. Aggregation

- Congress should affirm that States have authority to determine the terms and conditions of retail service, including the terms and conditions upon which aggregation is available.
- Congress should affirm that aggregators are subject to State licensing, registration and consumer protection requirements.

8. **RTO/Transmission Jurisdiction**

- 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 service. States should retain authority to establish retail transmission rates unless they violate federally-determined open-access, non-discriminatory, competitive transmission policies. FERC should continue to have ratemaking authority for interstate wholesale transactions. FERC should have jurisdiction over transactions between suppliers and retail customers located in different States and it should be required to defer to States acting on a regional basis.
- States should be primarily responsible for expeditiously handling retail complaints alleging undue discrimination in the marketplace. Appeals by market participants may be made to the FERC.
- NARUC supports legislation to authorize States to form voluntary regional bodies to address regional transmission system issues.
- NARUC supports legislation leading to voluntary formation of RTOs. Deference should be given to States in RTO development.
- Congress should develop a mechanism for States to address ongoing concerns in RTO functions after the initial RTO development period. These interests include reliability, market monitoring, pricing, congestion management, planning and interregional coordination. FERC should provide deference to States acting on a regional basis.
- Congress should provide for a State commission advisory role in RTO governance that allows deference to State commissions that reach consensus concerning these issues.
- NARUC supports an appropriate Federal role to resolve disputes between States.

9. **Consumer Protection**

- Congress should not preclude a State or State commission from prescribing and enforcing laws, regulations, or procedures regarding consumer protection.
- States should be given the latitude to prescribe consumer protection measures that are more prescriptive than Federal requirements.
- Congress should provide that aggregated consumer information should be made available by the local distribution company to other electric suppliers upon request and payment of a reasonable fee. However, any retail customer who believes that disclosure of such aggregated information would reveal energy use information of a competitively sensitive nature has the right to request the local distribution company not disclose such information. Congress should affirm that any consumer privacy disputes are to be resolved by the State Commission using its own consumer protection.
- NARUC supports State authority to ensure that retail electric competition does not result in the loss or degradation of service to rural, residential, or low-income consumers.

10. **PUHCA**

- NARUC supports reform or repeal of PUHCA as competition becomes effective under comprehensive legislation.
- NARUC supports a 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

11. **PURPA**

- 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.
- NARUC opposes FERC authority to order the recovery of costs in retail rates or to otherwise limit State authority to require mitigation of PURPA contract costs. States that originally approved these contracts are in a better position to address this issue than FERC.

12. **Public Benefits**

- Preservation of public benefits should be part of federal restructuring legislation.
- NARUC has identified many options to preserve public benefits. However, NARUC believes the best approach for Congress to follow during the transition to a competitive market is to establish a Federal/State trust, funded by a non-bypassable, competitively neutral customer charge. The fund could be administered by an independent entity.
- A State would qualify for the Federal match by designating its own program and funding mechanism for its match.

13. **Distributed Generation/Net Metering**

- NARUC supports Congress requiring the establishment of national interconnection and power quality standards, developed and adopted by appropriate technical standards organizations, such as the Institute of Electrical and Electronics Engineers, Inc., for facilities by a date certain.
- The States should have the flexibility to adopt these rules or their own rules.
- NARUC supports removing barriers to State implementation of net metering.

APPENDIX D

Resolution in Support of Customer "Right-to-Know" and Product Labeling Standards for the Retail Marketing of Electricity

WHEREAS, At least 30 million consumers in six States will begin choosing among competitive electricity providers in early 1998 and retail access to competing electricity suppliers is under consideration in many other states; and

WHEREAS, Electricity purchases make up a significant portion of the budget of many households; and

WHEREAS, The production of electricity imposes very substantial resource and environmental impacts; and

WHEREAS, Pilot retail access programs have shown that customer confusion and misleading claims are highly likely; and

WHEREAS, Clear and uniform disclosure may promote efficiency through informed product comparisons; and informed customer choice cannot occur in a retail electricity market without full disclosure of all relevant and important facts; and

WHEREAS, The desirability and feasibility of such disclosure is clearly established in nutrition labeling, uniform food pricing, truth-in-lending and many other Federal consumer protection programs; and

WHEREAS, The National Association of Regulatory Utility Commissioners (NARUC), at its November 1994 meeting, adopted a resolution on competition and stranded benefits calling for new proposals to preserve environmental and diversity benefits in a more competitive marketplace; and

WHEREAS, The NARUC, at its July 1996 meeting, adopted "Principles to Guide the Restructuring of the Electric Industry," which include market-based mechanisms to promote effective consumer choice and to preserve renewable resources, resource diversity and environmental protection; now, therefore, be it

RESOLVED, That the National Association of Regulatory Utility Commissioners (NARUC), convened at its 108th Annual Convention in San Francisco, California believes that restructuring the electric industry should facilitate informed customer choice that will promote efficient markets, resource diversity and environmental quality; and be it further

RESOLVED, That the NARUC supports initiatives leading to minimum, enforceable uniform standards for the form and content of disclosure and labeling that would allow retail and wholesale consumers to easily compare price, price variability, resource mix and environmental characteristics of their electricity purchases; and be it further

RESOLVED, That NARUC urges States adopting retail direct access programs to include enforceable standards of disclosure and labeling that would allow retail customers easily to compare the price, price variability, resource mix and environmental characteristics of their electricity purchases.

Sponsored by the Committee on Energy Conservation
Adopted November 20, 1996

APPENDIX E

NARUC RESPONSE TO CHAIRMAN BLILEY, HOUSE COMMERCE COMMITTEE MAY 16, 2000

1. Your letter, among others, raises concerns about Federal/State jurisdictional boundaries. Many other respondents felt that the jurisdictional boundaries between Federal and State regulators need further clarification. Please explain NARUC's interpretation of the provisions resolving Federal/State jurisdictional issues and the respective jurisdictions of Federal and State regulators?

   <u>Answer</u>: The following is NARUC's understanding of section 101 of H.R. 2944's resolution of Federal/State jurisdictional issues:

   a) Existing State authority to determine whether to require retail competition through unbundling of transmission and local distribution service is preserved (§ 101(a));
   b) FERC authority is extended to retail transmission services that are unbundled (§ 101(b));
   c) Existing State authority over all other retail services, including bundled sales, local distribution component of an unbundled sale, and the retail sale itself (i.e. the commodity) in the case of an unbundled sale is preserved (§ 101(b));
   d) Existing State authority to establish delivery charges to fund a list of public purposes is preserved (§ 101(d));
   e) Authority claimed by FERC in Order No. 888 to determine the character of power delivery facilities (i.e. whether transmission or distribution) is codified (§ 101(e));
   f) Existing State authority over retail sales and/or distribution services provided to U.S. government facilities is preserved (§ 101(f))

   NARUC believes that a workable and effective resolution of Federal/State jurisdictional issues is critically important to any restructuring legislation. Indeed, NARUC has worked extensively on the subject of jurisdiction since FERC adopted Order No. 888. At its last meeting in March, NARUC adopted by resolution (attached hereto) a model which bridges the gaps between the present jurisdictional divide and provides for both efficiency and nondiscrimination in the market while avoiding centralizing further authority in the Federal government at the expense of the States and of retail customers. Our position represents significant recognition by NARUC that States must not interfere with wholesale open access on a non-discriminatory basis and need to effectuate nondiscriminatory retail access for those States that have moved to full customer choice. On the other hand, it avoids FERC having to becoming embroiled in the complexity of setting transmission rates for individual retail customer classes (each of whom have peak usage of the transmission system at different times of the day and different seasons of the year), avoids citizens having to come to Washington for resolution of transmission rate or service issues and allows the States the flexibility they need to tailor electricity policy to their specific regional needs subject to an overall arching federal open access policy. It also would avoid the significant rate shifting (and resulting impact on State tax revenues) that would definitely occur should FERC be provided jurisdiction over retail transactions, whether bundled or unbundled. Such rate shifting and tax revenue losses would occur as a result of substituting FERC-determined wholesale rates for the present transmission rates embedded in bundled retail rates, each of which differ by customer class. By definition, substituting a "one size fits all" rate for the different retail rates presently paid by retail customers will lead to rate shifting among customer classes, among different utilities within a State and potentially by region.

   NARUCs proposal would provide for State jurisdiction over all deliveries of electricity over transmission lines, whether bundled or unbundled while FERC would maintain exclusive jurisdiction over wholesale sales. A State would have to follow policies of nondiscrimination and guidelines established by federal legislation as interpreted by FERC. This is similar to models which the Congress already established to address jurisdiction both in the Public Utilities Regulatory Policy Act of 1978 and most recently in the Telecommunications Policy Act of 1996.

NARUC would further agree to a "FERC backstop" appellate process which would be available to any party who felt that the State's actions was in violation of the nondiscrimination open access policies of federal law.

NARUC intends to work with all parties on the specific legislative language. One potential construct of this language would be as follows:

"FERC shall not exercise authority over retail transmission service except to resolve complaints alleging discrimination in the application of the open access provisions of this Act by a particular State. States that have adopted open access retail policies shall ensure open, nondiscriminatory use of the transmission systems within their State for deliveries of electricity for resale to retail customers in accordance with State law and the requirements of this legislation."

2. Chairman Hoecker’s comments on H.R. 2944 stated that “H.R. 2944 fails to adequately address the jurisdictional problem evidenced by the Eighth Circuit’s recent holding in Northern State’s Power Co. v. FERC? .” Do you agree or disagree? How should Federal legislation address this issue?

Answer: NARUC is unaware of any provisions included in H.R. 2944 that were specifically intended to address the holding in this case that the Federal Power Act does not provide FERC jurisdiction to “regulate the curtailment of electric transmission on native/retail consumers? .” However, to the extent that section 101 of H.R. 2944 provides FERC authority over transmission services provided retail consumers on an unbundled basis, the legislation would change the result in the NSP case as to those services.

NARUC supported the result in this case when it was on rehearing at the Court of Appeals. It is our view that any legislation Congress enacts should affirm State authority to regulate retail power delivery services. As our answer to Question 1 describes, if such authority is exercised in ways that cause undue discrimination against market participants – including the authority to regulate retail curtailment policies – then FERC should have authority to act to remove such discrimination.

3. Does NARUC believe that requiring utilities to unbundle transmission rates will force a State to move to retail competition? Is it possible for a utility in a State that does not have retail competition to completely unbundle its transmission services?

Answer: Requiring utilities to unbundled transmission will not – as a matter of law – automatically force States to move to retail competition provided that the legislation makes clear that that is not Congress’ intent. It is possible for a utility in a State without retail competition to provide transmission services on an unbundled basis.

NARUC opposes federal legislation that would force States to unbundle retail service and transfer jurisdiction over retail transmission service to FERC, other than the appellate-type authority described in our answer to Question 1.

4. FERC issued Order 2000 urging the formation of voluntary Regional Transmission Organizations (RTOs) after Subcommittee action on H.R. 2944. What is NARUC’s position on that rule? Do you believe that there is a need for independent operation of the interstate transmission grid to assure competition in wholesale markets? Are States in a position to assure that independence?

Answer: As a general matter, NARUC supports Order No. 2000. We support independence as a hallmark of RTO policy. Working with FERC, States can help assure independence as part of the process of implementing Order No. 2000. However, there is a threat to State action in this area based upon recent utility claims that State efforts to encourage or direct utilities to join a given RTO, and to establish conditions on their participation, are preempted by FERC’s “exclusive jurisdiction” over transmission services and facilities. We recommend that Congress clarify that nothing in Federal law works to defeat State actions that support Federal policies favoring the development of FERC-jurisdictional RTOs. For example, a number of States such as Ohio and Virginia have adopted policies as an element of their retail restructuring initiatives that require utilities to participate in RTOs. We urge Congress to support and facilitate these kinds of pro-competitive State policies.

5. Is it possible for efficient and effective RTO's to form if States retain jurisdiction over bundled transmission services and rates?

   Answer: NARUC believes that it is possible for efficient and effective RTO's to focus on wholesale transmission services notwithstanding State jurisdiction at the retail level. The benefit of preserving State jurisdiction is to enable State commissions to take local needs into account. As Order No. 2000 is implemented, regionalism will continue to grow in importance. Accordingly, NARUC strongly supports the parallel development of cooperative regional regulatory mechanisms to support non-discriminatory, open-access transmission services.

6. Chairman Hoecker's comments on H.R. 2944 highlight that H.R. 2944 would limit FERC's authority to undertake the initiatives contained in Order 2000. Is that your interpretation? Would you support modifying H.R. 2944 to make clear that FERC's Order 2000 could be implemented?

   Answer: We do not believe that the legislation unnecessarily limits FERC's authority to implement the Commission's overarching policy of non-discriminatory access to wholesale transmission services through the development of RTOs. However, as noted, NARUC supports Order No. 2000, and accordingly, we believe Congress should consider appropriate amendments deemed necessary to facilitate implementation of that order.

7. H.R. 2944 places a 180 day time limit on FERC's consideration of mergers. Some respondents argued that such a limit would result in FERC arbitrarily rejecting mergers based upon inadequate time for full consideration of the merger proposal. Does NARUC support the time limit on merger consideration?

   Answer: NARUC does not support a strict time limit. The legislation should enable FERC to extend any statutory review period for good cause.

8. Does NARUC support the provisions regarding transmission expansion currently contained in H.R. 2944?

   Answer: In March, NARUC adopted its position on siting of expanded transmission capacity which "supports voluntary regional bodies to address siting" issues. We further stated that "Congress should provide an explicit grant of authority to the States and FERC to act in cooperation" in this area. "Congress should affirm that States have the primary authority to set up, operate and govern these voluntary regional siting bodies, and FERC would act as an appropriate 'backstop' authority where States or regions fail to act." Provisions of section 105 of H.R. 2944 that would authorize joint boards appear to address the same need for coordinated multistate action.

   We believe that the position adopted by our Association in March represents a significant step for NARUC to take to develop a workable compromise on the siting issue, particularly with respect to the role that FERC would play in cases where State and regional siting decisions are not forthcoming.

9. NARUC has expressed some concerns about the consensus reliability language contained in H.R. 2944. Please provide legislative language that would address NARUC's concerns.

   Answer: NARUC cannot support the so-called "consensus" reliability language developed by the North American Electric Reliability Council (NERC) as reflected in H.R. 2944 without amendment to provide an explicit and appropriate role for the States. To that end, we advocate the addition of two amendments (attached hereto). The first is a "savings" clause to clarify that existing State authority to ensure reliable service is not preempted by the NERC legislation unless a State's action is found by FERC to have a material adverse impact on reliability of the bulk power system or is greater than necessary to meet the State's reliability needs. The second is an amendment to allow States to form regional advisory bodies (with deference from FERC when acting on an interconnection-wide basis) to address reliability standards. With these amendments, provisions in H.R. 2944 with respect to the New York State Reliability Council and State authority over reliability of the distribution network are unnecessary and should be deleted.

Given the increasing attention that the States, FERC, Congress and the Administration have given to reliable electric service, we wish to make very clear that NARUC has worked diligently with NERC (and for that matter, all other stakeholder groups that are interested in finding a solution on this issue) to find a compromise that recognizes the legitimate interest of the States in ensuring reliable service of the electrical systems and facilities now being used to support expanding commercial activities. In our view, the amendments we have attached reflect significant movement in the direction of a workable compromise – movement we have yet to see from other participants in this debate.

10. Your letter expresses support for provisions that grandfather State programs. Could you describe NARUC's interpretation of H.R. 2944's grandfathering provisions? How do the grandfathering provisions work in relation to the Federal/State jurisdictional boundaries drawn by the legislation?
Answer: There appear to be at least two grandfather provisions in H.R. 2944. Section 3 states "that any State law or regulatory order adopted before the date three years after the date of enactment" shall be grandfathered, provided that the law or order addresses consumer protection issues covered by Title III, interconnection issues covered by section 532, aggregation issues covered by section 219 and net metering issues covered by section 702. Section 107(b) is a savings clause stating that nothing in the legislation preempts "any State retail access plan" adopted or implemented within three years of enactment.

In relation to "the Federal/State jurisdictional boundaries drawn by the legislation," Section 3 acts as a limit on the application of Federal law to State decisions in the four listed areas – consumer protection, interconnection, aggregation and net metering – that are adopted within 36 months of the date of enactment. State-jurisdictional utilities would be required to comply with State decisions made during the three-year period, notwithstanding Federal requirements in these areas.

Section 107(b) would constitute a rule of construction to be used by a court reviewing a State commission requirement (that is part of the State's retail access plan) that is alleged to implicate a provision of the Federal Power Act as amended by this legislation. The purpose of this kind of savings clause is to make clear to reviewing courts that Congress does not intend that the Federal legislation "occupies the field." In the case of this formulation, this means that as a general matter, utilities subject to State regulatory jurisdiction must comply with State requirements found in a retail access plan unless compliance with the Federal Power Act makes it impossible to do so. A party objecting to the State requirement would bear the burden of proof on this issue.

11. Your letter expresses support for a "State-Federal partnership to support State and utility public benefits funds? " Please provide specific legislative language that you would support on this issue.

Answer: In its March resolution, NARUC adopted a more detailed statement of its policy on public benefits legislation that establishes "a Federal/State trust, funded by a non-bypassable, competitively neutral customer charge." The fund would be administered by an independent entity, and participating States would qualify for Federal matching funds "by designating its own program and funding mechanism for its match." We are working to develop specific legislative provisions to implement this policy. Generally patterned after S. 1369, introduced by Senator Jeffords, this amendment will be provided to the Committee as soon as we've completed our work.

12. H.R. 2944 is silent with respect to privacy issues. Does NARUC have a position on privacy issues?

Answer: In its March resolution (attached), NARUC adopted the following position on consumer privacy and information disclosure: "Congress should provide that aggregated consumer information should be made available by the local distribution company . . . upon request and payment of a reasonable fee." A retail customer that believes disclosure by his or her distribution company will cause competitive harm should be able to request that information not be disclosed. Disputes over the release of information should be resolved under State commission policies and procedures.

In fact, Section 302 of H.R. 2944 would establish consumer privacy rules under the administration of the Federal Trade Commission. This section would prohibit the disclosure of customer-specific information without the customer's "prior written approval." This "opt-in" provision is generally consistent with NARUC's approach both with respect to electricity issues, but also telecommunications issues.

However, there are two other aspects of Section 302 that are troublesome: first, section 302(c) (dealing with disclosure of aggregated customer information) should allow customers to petition their distributor to block the release of aggregate information that is competitively sensitive; i.e. if a given customer's information is discernible from the aggregated data and its disclosure would affect the customer's competitive position.

Second, section 302(e) should be amended to make clear that State requirements that are more prescriptive or provide greater consumer protection are not preempted. We believe that Congress should make clear that such State requirements are allowed by deleting the "not inconsistent" language of this subsection. Specifically, we recommend that the first sentence of section 302(e) be revised by deleting the phrase "so long as such laws, regulations, or procedures are not inconsistent with the provisions of this section or with any rule prescribed by the Federal Trade Commission pursuant to it."

13. Please explain NARUC's position with respect to inclusion of uniform interconnection standards in Federal legislation? Does NARUC support the development of uniform interconnection standards? Please provide the authorizing language NARUC requests in its letter to "give States the authority to implement interconnection policies that make sense for the unique circumstances that individual States confront."

<u>Answer</u>: NARUC supports congressional legislation that requires the establishment of national interconnection and power quality standards, developed and adopted by appropriate technical standards organizations, such as the Institute of Electrical and Electronics Engineers, Inc., by a date certain. We further believe that the legislation should place the responsibility for implementation of these standards at the State level, and further, should permit States to adopt or modify the standards to meet local needs. We have not yet developed specific legislative language to implement this position.

14. Your letter is silent with respect to aggregation. What is NARUC's position with respect to aggregation provisions in H.R. 2944?

<u>Answer</u>: Section 531 of H.R. 2944 adds a new Section 219 to the FPA, creating a Federal right of aggregation. This provision is only partially consistent with NARUC's position, reflected in the attached policy resolution adopted in March of this year, that States should have the authority to determine "the terms and conditions upon which aggregation is available," and further, that Congress should affirm "that aggregators are subject to State licensing, registration and consumer protection requirements." We recommend that Section 219 be revised to specify that these State policies are not preempted through the amendment of the first sentence as follows:

"Subject to not unduly discriminatory or preferential State requirements, *including licensing, registration and consumer protection laws and regulations,* each retail electric consumer may designate ...."

Additional language in italics.

15. Your letter states NARUC "supports further consultation between Federal agencies and State commissions to produce enforceable uniform standards for information disclosure and product labeling." Please elaborate. How would the grandfathering provisions affect such a standard?

<u>Answer</u>: NARUC has worked with the U.S. Department of Energy to develop model information disclosure policies for implementation by the States. To date, [number] of States that have opened their markets to retail competition have adopted this model. Under the grandfather provision of section 3, States that have adopted this model (either prior to or within three years of enactment) would be free to continue implementing and enforcing this policy.

16. Your letter seems to express support for Federal legislation with respect to "slamming" and "cramming" as long as it allows States to implement more stringent consumer protection policies. Is

this a correct interpretation of NARUC's position? Would the grandfathering provisions of H.R. 2944 prohibit enforcement of, or allow States to "opt out" of enforcement of Federal "slamming" and "cramming" laws within their jurisdiction?"

Answer: As a general matter, NARUC believes that congressional legislation in the area of consumer protection – including remedies for slamming and cramming – should provide that States are free to prescribe and implement enforcement policies that "are more prescriptive than Federal requirements." States are the first line of defense against consumer fraud and abuse. As we have learned in telecommunications and as we are learning in energy restructuring, NARUC's member commissions, along with State attorneys general, are the agencies that consumers call for assistance, that handle complaints, and that must provide necessary remedies against firms that will not comply with legal requirements. Any legislation developed by Congress in this area must preserve the front-line role of the States.

Concerning the effect of the grandfather provisions in this area, it would appear that section 3 of H.R. 2944 means that in a grandfathered State, all entities (including utilities, consumers, marketers etc.) would be governed by State law and procedures in grandfathered areas (consumer protection, interconnection, aggregation and net metering) rather than a Federal standard established under the corresponding provisions of the legislation.

17. Please elaborate on your position on the repeal of PUHCA and PURPA. What legislative proposals would NARUC offer to modify those provisions in H.R. 2944?

Answer: Concerning PUHCA, NARUC supports reform or repeal of the statute as competition becomes effective under comprehensive legislation. We also support State and FERC access to holding company books and records and preservation of consumer protection provisions of the 1992 Energy Policy Act and 1996 Telecommunications Act (as codified in the attached amendatory provision).

Concerning PURPA, NARUC supports legislation to remove the statute's mandatory purchase requirement where a State has determined that generating markets are competitive or that the public interest in resource acquisition is protected. NARUC opposes legislative provisions that give FERC authority to order the recovery of PURPA contract costs or otherwise preempt State authority.

18. With respect to market power, your letter states that "the States are capable of resolving market power issues, provided legislation clarifies that State regulators have the authority to do so." Please provide legislative language that you believe achieves this result.

Answer: NARUC would offer the following language as an amendment to Section 101(a) of H.R. 2944 adds to section 201(b) of the Federal Power Act:

"This Act shall not affect the authority of a State or municipality to require retail electric competition, or to require the unbundling of transmission and local distribution service for the delivery of electric energy directly to a retail electric consumer *or to investigate the alleged abuse of market power by any entity subject to the regulatory jurisdiction of the State and impose any remedy for such abuse provided under State law*."

Additional language in italics.

APPENDIX F

Resolution Regarding Cost Allocation Guidelines for the Energy Industry

WHEREAS, There is ongoing concern regarding potential cross-subsidization between the regulated monopoly operations and the non-regulated businesses of electric and gas utilities; and

WHEREAS, Utilities are adopting various business strategies to adjust to the changing retail markets, including forming alliances and creating subsidiaries, divisions and partnerships to participate in non-regulated, competitive markets; and

WHEREAS, State utility commissions are examining and adopting various policies to monitor the competitive activities of regulated energy utilities; and

WHEREAS, State utility commissions are examining and adopting policies and rules concerning potential cross-subsidies between regulated utilities and non-regulated affiliates including pricing of assets, products and services; and

WHEREAS, The National Association of Regulatory Utility Commissioners (NARUC) requested the Staff Subcommittee on Accounts together with the Staff Subcommittees on Strategic Issues and Gas to prepare for NARUC's consideration, "Guidelines for Energy Cost Allocations"; and

WHEREAS, The Staff Subcommittee on Accounts together with the Subcommittee on Gas and Strategic Issues have prepared for NARUC's consideration "Guidelines for Cost Allocations and Affiliate Transactions"; and

WHEREAS, Each State or Federal Regulatory commission may have unique situations and circumstances that govern affiliate transactions, cost allocations, and/or service or product pricing; and

WHEREAS, The "Guidelines for Cost Allocations and Affiliate Transactions" are to provide guidance to the states and are not intended to be rules or regulations prescribing how cost allocations and affiliate transactions are to be handled; and

WHEREAS, The Staff Subcommittees on Accounts, Strategic Issues and Gas should periodically review the Guidelines for Cost Allocations and Affiliate Transactions, taking into consideration the progression of competition in the electric and gas industries nationally, and report their findings, including proposed changes to the guidelines, if necessary, that promote efficiency in competitive energy markets while guarding against cross-subsidization by monopoly ratepayers; *now therefore be it*

RESOLVED, The Board of Directors of the of the National Association of Regulatory Utility Commissioners (NARUC), convened in its 1999 Summer Meeting in San Francisco, California, adopts the attached "Guidelines for Cost Allocations and Affiliate Transactions"; *and be it further*

RESOLVED, The NARUC directs the Staff Subcommittees on Accounts, Strategic Issues and Gas, to review the Guidelines for Cost Allocation and Affiliate Transactions, taking into consideration the progression of competition in the electric and gas industries nationally and report their findings to NARUC, including proposed changes to the guidelines, if necessary, on or before January 1, 2001, and annually thereafter, *and be it further*

RESOLVED, The NARUC applauds and thanks the Staff Subcommittees on Accounts, Gas, and Strategic Issues for their excellent work in developing the guidelines.

Sponsored by the Committees on Electricity and Finance and Technology
Adopted by the NARUC Board of Directors July 23, 1999

***Attachment To Resolution Regarding Cost Allocation Guidelines for the Energy Industry* "GUIDELINES FOR COST ALLOCATIONS AND AFFILIATE TRANSACTIONS"**

The following Guidelines for Cost Allocations and Affiliate Transactions (Guidelines) are intended to provide guidance to jurisdictional regulatory authorities and regulated utilities and their affiliates in the development of procedures and recording of transactions for services and products between a regulated entity and affiliates. The prevailing premise of these Guidelines is that allocation methods should not result in subsidization of non-regulated services or products by regulated entities unless authorized by the jurisdictional regulatory authority. These Guidelines are not intended to be rules or regulations prescribing how cost allocations and affiliate transactions are to be handled. They are intended to provide a framework for regulated entities and regulatory authorities in the development of their own policies and procedures for cost allocations and affiliated transactions. Variation in regulatory environment may justify different cost allocation methods than those embodied in the Guidelines.

The Guidelines acknowledge and reference the use of several different practices and methods. It is intended that there be latitude in the application of these guidelines, subject to regulatory oversight. The implementation and compliance with these cost allocations and affiliate transaction guidelines, by regulated utilities under the authority of jurisdictional regulatory commissions, is subject to Federal and state law. Each state or Federal regulatory commission may have unique situations and circumstances that govern affiliate transactions, cost allocations, and/or service or product pricing standards. For example, The Public Utility Holding Company Act of 1935 requires registered holding company systems to price "at cost" the sale of goods and services and the undertaking of construction contracts between affiliate companies.

The Guidelines were developed by the NARUC Staff Subcommittee on Accounts in compliance with the Resolution passed on March 3, 1998 entitled "Resolution Regarding Cost Allocation for the Energy Industry" which directed the Staff Subcommittee on Accounts together with the Staff Subcommittees on Strategic Issues and Gas to prepare for NARUC's consideration, "Guidelines for Energy Cost Allocations." In addition, input was requested from other industry parties. Various levels of input were obtained in the development of the Guidelines from the Edison Electric Institute, American Gas Association, Securities and Exchange Commission, the Federal Energy Regulatory Commission, Rural Utilities Service and the National Rural Electric Cooperatives Association as well as staff of various state public utility commissions.

In some instances, non-structural safeguards as contained in these guidelines may not be sufficient to prevent market power problems in strategic markets such as the generation market. Problems arise when a firm has the ability to raise prices above market for a sustained period and/or impede output of a product or service. Such concerns have led some states to develop codes of conduct to govern relationships between the regulated utility and its non-regulated affiliates. Consideration should be given to any "unique" advantages an incumbent utility would have over competitors in an emerging market such as the retail energy market. A code of conduct should be used in conjunction with guidelines on cost allocations and affiliate transactions.

A. DEFINITIONS

1. Affiliates **-** companies that are related to each other due to common ownership or control.

2. Attestation Engagement **-** one in which a certified public accountant who is in the practice of public accounting is contracted to issue a written communication that expresses a conclusion about the reliability of a written assertion that is the responsibility of another party.

3. Cost Allocation Manual (CAM) **-** an indexed compilation and documentation of a company's cost allocation policies and related procedures.

4. Cost Allocations **-** the methods or ratios used to apportion costs. A cost allocator can be based on the origin of costs, as in the case of cost drivers; cost-causative linkage of an indirect nature; or one or more overall factors (also known as general allocators).

5. Common Costs - costs associated with services or products that are of joint benefit between regulated and non-regulated business units.

6. Cost Driver - a measurable event or quantity which influences the level of costs incurred and which can be directly traced to the origin of the costs themselves.

7. Direct Costs - costs which can be specifically identified with a particular service or product.

8. Fully Allocated costs - the sum of the direct costs plus an appropriate share of indirect costs.

9. Incremental pricing - pricing services or products on a basis of only the additional costs added by their operations while one or more pre-existing services or products support the fixed costs.

10. Indirect Costs - costs that cannot be identified with a particular service or product. This includes but not limited to overhead costs, administrative and general, and taxes.

11. Non-regulated - that which is not subject to regulation by regulatory authorities.

12. Prevailing Market Pricing - a generally accepted market value that can be substantiated by clearly comparable transactions, auction or appraisal.

13. Regulated - that which is subject to regulation by regulatory authorities.

14. Subsidization - the recovery of costs from one class of customers or business unit that are attributable to another.

B. COST ALLOCATION PRINCIPLES

The following allocation principles should be used whenever products or services are provided between a regulated utility and its non-regulated affiliate or division.

1. To the maximum extent practicable, in consideration of administrative costs, costs should be collected and classified on a direct basis for each asset, service or product provided.

2. The general method for charging indirect costs should be on a fully allocated cost basis. Under appropriate circumstances, regulatory authorities may consider incremental cost, prevailing market pricing or other methods for allocating costs and pricing transactions among affiliates.

3. To the extent possible, all direct and allocated costs between regulated and non-regulated services and products should be traceable on the books of the applicable regulated utility to the applicable Uniform System of Accounts. Documentation should be made available to the appropriate regulatory authority upon request regarding transactions between the regulated utility and its affiliates.

4. The allocation methods should apply to the regulated entity's affiliates in order to prevent subsidization from, and ensure equitable cost sharing among the regulated entity and its affiliates, and vice versa.

5. All costs should be classified to services or products which, by their very nature, are either regulated, non-regulated, or common to both.

6. The primary cost driver of common costs, or a relevant proxy in the absence of a primary cost driver, should be identified and used to allocate the cost between regulated and non-regulated services or products.

7. The indirect costs of each business unit, including the allocated costs of shared services, should be spread to the services or products to which they relate using relevant cost allocators.

C. COST ALLOCATION MANUAL (NOT TARIFFED)

Each entity that provides both regulated and non-regulated services or products should maintain a cost allocation manual (CAM) or its equivalent and notify the jurisdictional regulatory authorities of the CAM's existence. The determination of what, if any, information should be held confidential should be based on the statutes and rules of the regulatory agency that requires the information. Any entity required to provide notification of a CAM(s) should make arrangements as necessary and appropriate to ensure competitively sensitive information derived therefrom be kept confidential by the regulator. At a minimum, the CAM should contain the following:

1. An organization chart of the holding company, depicting all affiliates, and regulated entities.

2. A description of all assets, services and products provided to and from the regulated entity and each of its affiliates.

3. A description of all assets, services and products provided by the regulated entity to non-affiliates.

4. A description of the cost allocators and methods used by the regulated entity and the cost allocators and methods used by its affiliates related to the regulated services and products provided to the regulated entity.

D. AFFILIATE TRANSACTIONS (NOT TARIFFED)

The affiliate transactions pricing guidelines are based on two assumptions. First, affiliate transactions raise the concern of self-dealing where market forces do not necessarily drive prices. Second, utilities have a natural business incentive to shift costs from non-regulated competitive operations to regulated monopoly operations since recovery is more certain with captive ratepayers. Too much flexibility will lead to subsidization. However, if the affiliate transaction pricing guidelines are too rigid, economic transactions may be discouraged.

The objective of the affiliate transactions' guidelines is to lessen the possibility of subsidization in order to protect monopoly ratepayers and to help establish and preserve competition in the electric generation and the electric and gas supply markets. It provides ample flexibility to accommodate exceptions where the outcome is in the best interest of the utility, its ratepayers and competition. As with any transactions, the burden of proof for any exception from the general rule rests with the proponent of the exception.

1. Generally, the price for services, products and the use of assets provided by a regulated entity to its non-regulated affiliates should be at the higher of fully allocated costs or prevailing market prices. Under appropriate circumstances, prices could be based on incremental cost, or other pricing mechanisms as determined by the regulator.

2. Generally, the price for services, products and the use of assets provided by a non-regulated affiliate to a regulated affiliate should be at the lower of fully allocated cost or prevailing market prices. Under appropriate circumstances, prices could be based on incremental cost, or other pricing mechanisms as determined by the regulator.

3. Generally, transfer of a capital asset from the utility to its non-regulated affiliate should be at the greater of prevailing market price or net book value, except as otherwise required by law or regulation. Generally, transfer of assets from an affiliate to the utility should be at the lower of prevailing market price or net book value, except as otherwise required by law or regulation. To determine prevailing market value, an appraisal should be required at certain value thresholds as determined by regulators.

4. Entities should maintain all information underlying affiliate transactions with the affiliated utility for a minimum of three years, or as required by law or regulation.

E. AUDIT REQUIREMENTS

1. An audit trail should exist with respect to all transactions between the regulated entity and its affiliates that relate to regulated services and products. The regulator should have complete access to all affiliate records necessary to ensure that cost allocations and affiliate transactions are conducted in accordance with the guidelines. Regulators should have complete access to affiliate records, consistent with state statutes, to ensure that the regulator has access to all relevant information necessary to evaluate whether subsidization exists. The auditors, not the audited utilities, should determine what information is relevant for a particular audit objective. Limitations on access would compromise the audit process and impair audit independence.

2. Each regulated entity's cost allocation documentation should be made available to the company's internal auditors for periodic review of the allocation policy and process and to any jurisdictional regulatory authority when appropriate and upon request.

3. Any jurisdictional regulatory authority may request an independent attestation engagement of the CAM. The cost of any independent attestation engagement associated with the CAM, should be shared between regulated and non-regulated operations consistent with the allocation of similar common costs.

4. Any audit of the CAM should not otherwise limit or restrict the authority of state regulatory authorities to have access to the books and records of and audit the operations of jurisdictional utilities.

5. Any entity required to provide access to its books and records should make arrangements as necessary and appropriate to ensure that competitively sensitive information derived therefrom be kept confidential by the regulator.

F. REPORTING REQUIREMENTS

1. The regulated entity should report annually the dollar amount of non-tariffed transactions associated with the provision of each service or product and the use or sale of each asset for the following:

   a. Those provided to each non-regulated affiliate.

   b. Those received from each non-regulated affiliate.

   c. Those provided to non-affiliated entities.

2. Any additional information needed to assure compliance with these Guidelines, such as cost of service data necessary to evaluate subsidization issues, should be provided.

APPENDIX G

Resolution on Public Benefits

WHEREAS, The National Association of Regulatory Utility Commissioners ("NARUC") adopted in November 1994 a Resolution in Competition, the Public Interest, and Potentially Stranded Benefits which states "that 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;" and

WHEREAS, NARUC adopted in July 1995 a resolution setting out "Principles to Guide the Restructuring of the Electric Industry" which states, among other things, that "The public benefits of energy efficiency, renewable resource technologies and research and development should be maintained through existing or new mechanisms;" and

WHEREAS, The nation has a compelling interest in preserving and promoting these public benefits, for the good of consumers, the economy, and the environment; and

WHEREAS, NARUC adopted in November 1997 a *Resolution Endorsing Federal Legislative Provisions to Preserve and Promote Public Benefits Programs in the Nation's Electric Industry* that 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;" and

WHEREAS, The November 1997 Resolution also outlined design principles for such mechanisms that should be considered, including:

- A Federal-State partnership, building upon State and utility expertise in designing and implementing electric serve and public purpose program, 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 oversights; 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; and

WHEREAS, NARUC in March of 2000 adopted a Resolution Adopting Positions on Issues in Federal Legislation to Restructure the Electric Industry which included a statement regarding Public Benefits that "NARUC believes the best approach for Congress to follow during the transition to a competitive market is to establish a Federal/State trust funded by a non-bypassable, competitively neutral customer charge."; and

WHEREAS, The March 2000 Resolution also stated that "A State would qualify for the Federal Match by designating its own program and funding mechanism for its match"; *now therefore be it*

RESOLVED**, That the Board of Directors of the National Association of Regulatory Utility Commissioners ("NARUC") convened at its July 2000 Summer Meeting in Los Angeles, California, hereby re-affirms its insistence that Public Benefits must be included in any electric industry restructuring legislation, and be it further**

RESOLVED, That further study of societal costs and benefits is warranted prior to NARUC supporting any particular implementation or funding mechanism for the continued support of Public Benefit Programs**.**

Sponsored by the Committees on Electricity and Gas
Adopted by NARUC Board of Directors July 26, 2000

APPENDIX H

Resolution Relating to Market Power In A Restructured Electric Power Industry

WHEREAS, Some state and territorial legislatures and regulatory commissions, in considering legislation and developing policies to restructure the electric industry to introduce competition in retail power supply markets, have recognized that after-the-fact antitrust enforcement may not be sufficient to protect against market power abuses in the transition from monopoly to competitive markets; and

WHEREAS, Abuse of market power can diminish the economic gains to consumers from a restructured electric power industry, in which long-term consumer interests require that neither incumbents nor new entrants gain or retain unfair market advantage; and

WHEREAS, Abuse of market power may be avoided or mitigated by various governmental actions, ranging from behavioral rules and functional unbundling to structural separation and divestiture, with varying effects on consumers and firms; and

WHEREAS, Abuse of market power may stem from barriers to competition from a variety of sources, including barriers erected by incumbent firms; and

WHEREAS, The effectiveness of individual market-power mitigation actions depends on the unique circumstances surrounding a specific market area within which electric services are transacted; now, therefore, be it

RESOLVED, That the Executive Committee of the National Association of Regulatory Utility Commissioners (NARUC), convened at its 1998 Summer Meetings in Seattle, Washington, hereby states that Congress should not preempt jurisdiction in the States and territories to address market power concerns; and State and territorial legislatures should give clear and adequate authority to the State and territorial public utility commissions to protect all classes of consumers from the abuse of market power, including the authority to require behavioral and structural remedies to address excessive market power; and be it further

RESOLVED, That industry restructuring to achieve effective retail competition in electric supply should remove barriers to entry and allow open and nondiscriminatory access to essential network facilities; and be it further

RESOLVED, That restructuring designed to open competitive electricity markets should protect consumers against the abuses resulting from the exercise of market power; and be it further

RESOLVED, That any market-power remedies should weigh the benefits and costs, including reliability impacts and economies of scale and scope, from the perspective of all classes of electricity consumers; and be it further

RESOLVED, That NARUC advocates a continuum of options for the mitigation of market power, and urges State and territorial legislatures and Congress, in considering restructuring, to preserve State and territorial flexibility to use these options as needed. Legislation should clarify the authority to use accounting conventions and codes of conduct, which may be sufficient safeguards in some cases. 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, and to impose affiliate transaction and other rules to assure that electric customers do not subsidize non-utility ventures. Legislation should clarify that States and territories have clear authority to require the formation of appropriate state, territory, 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 authorized to require divestiture where appropriate and necessary; and be it further

RESOLVED, That governmental agencies, including State and territorial commissions, the United States Department of Justice, the Federal Trade Commission, State and territorial attorneys general, and the FERC, should cooperate in monitoring, preventing, and correcting excessive market power in the electric power industry, with attention to market concentration, entry barriers, collusion, and other anti-competitive activities; and be it further

RESOLVED, That in providing critical tools to assist State and territorial regulators in addressing market power, 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.

Sponsored by the Committees on Electricity, Energy Resources,
Finance and Technology, and Gas
July 98

APPENDIX I

Resolution Regarding Equal Consideration
Of Demand and Supply Responses in Electric Markets

WHEREAS, The Federal Energy Regulatory Commission is actively considering which entities should be responsible for the efficient construction and reinforcement of the transmission system in a competitive wholesale market; and

WHEREAS, The Federal Energy Regulatory Commission is also reviewing pricing policies that will lead to the efficient siting of new generation resources in competitive wholesale markets; and

WHEREAS, Several states have passed legislation and implemented rules to permit customer choice among energy providers; and

WHEREAS, Competitive energy providers may wish to offer their customers products which react to prices available in the wholesale markets; and

WHEREAS, Customer options may include demand reductions and load shifting in response to those price signals; and

WHEREAS, When supplies are constrained, markets will be most competitive where customers are able to react to prices; and

WHEREAS, Reaction to such price signals can offer greater public benefits by mitigating market power, furthering innovation, easing transmission and distribution constraints, increasing diversity, encouraging reductions in unnecessarily costly energy usage, and improving reliability; *now therefore be it*

RESOLVED, That the Board of Directors of the National Association of Regulatory Utility Commissioners ("NARUC"), convened in its 2000 Summer Meeting in Los Angeles, California, finds that, in remedying situations of inadequate supply or constrained transmission, demand responses to market prices should be equally and fairly compared to alternatives which require the construction of new transmission or generation; *and be it further*

RESOLVED, That NARUC urges the FERC to include mechanisms which permit market-driven consumer responses to shortages in its decisions regarding the need for generation and transmission improvements, and to facilitate such responses by encouraging the development of wholesale markets which convey appropriate price signals to end-use customers.

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Sponsored by the Committee on Energy Resources and the Environment
Adopted by the NARUC Board of Directors July 26, 2000

APPENDIX J

Resolution Regarding Interconnection Standards for Small-Scale Generating Facilities

WHEREAS, Advances in smaller-scale generation options have played a significant role in the move to restructure electricity markets; and

WHEREAS, Access to the electric supply market by small-scale distributed resources can offer public benefits by mitigating market power, furthering innovation, easing transmission and distribution constraints, increasing resource diversity, and expanding customer choice; and

WHEREAS, Certain small-scale generating units, such as co-generating units, micro-turbines, and fuel cells, have reduced air emissions and have achieved high efficiencies; and

WHEREAS, Certain of these resources use renewable fuels, the promotion of which has been an important national goal under past utility regulatory policy, including the Public Utility Regulatory Policies Act of 1978 and the Energy Policy Act of 1992; and

WHEREAS, Utility-specific interconnection rules currently constitute a significant barrier to the effective use of small-scale, distributed generating units, raising costs for customers, marketers and developers, and increasing the costs, administrative burdens, and market entry barriers to interconnect these resources; and

WHEREAS, There are a number of important interconnection issues related to safety and reliability that could be developed into uniform standards; now, therefore, be it

RESOLVED, That the Executive Committee of the National Association of Regulatory Utility Commissioners (NARUC), convened at its 1998 Summer Committee Meetings in Seattle, Washington, finds that greater consistency in the terms and conditions of interconnection of small-scale generating units lowers market entry barriers and allows the industry and the public to realize the benefits from the effective use of small-scale facilities; and be if further

RESOLVED, That the NARUC urges State commissions to remove any unnecessary barriers to interconnection of small-scale generating units; and be it further

RESOLVED, That the NARUC supports further exploration of issues relating to the interconnection of small-scale generators and to the regulation of distribution systems that affect market entry of distributed small-scale generation.

Sponsored by the Committees on Energy Resources and Electricity
July 98