Utilities Want it Both Ways, ELCON Tells FERC in Market Power Petition

They Claim Screens Are Inadequate After Failing Them

ELCON filed three motions to intervene at the Federal Energy Regulatory Commission in cases involving utilities that continue to seek market-based rates despite their inability to comply with an April 14 FERC order on mitigation of market power.

The motions urged FERC to initiate a Section 206 investigation against Southern Company, Entergy, and AEP unless each utility offers a plan for market power mitigation.

“FERC issued its order pursuant to public law,” said ELCON Executive Director John Anderson. "A utility should not be allowed to disregard a FERC order -- that's equivalent to disregarding public law. We are urging FERC to stand firm and to begin the investigations. If they allow utilities to subvert the law and continue to exercise market power, it's a bad day for consumers. And it's a terrible day...

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NYISO Demand Curve Proposal Should Be Rejected, Industrials Tell Court

ELCON and several other industrial electricity users asked the U.S. Court of Appeals for the D.C. Circuit to reject the Federal Energy Regulatory Commission's approval of the New York ISO's unproven proposal to increase generation.

Even FERC admits it will raise rates, the petitioners noted.

“The New York ISO's so-called Demand Curve plan will not accomplish its stated objective -- which is increased generation -- but even FERC admits that it is a novel and experimental proposal that will increase costs for end users,” ELCON Executive Director John Anderson asserted. “And it will also -- unnecessarily -- increase profits for generators.”

The New York ISO's installed capacity (ICAP) Demand Curve proposal administratively sets a clearing price for generated

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ELCON to NERC: Examine Council Roles

In a world of regional transmission organizations (RTOs) and large, competitive markets, it is time for the North American Electric Reliability Council (NERC) to examine whether its regional reliability councils fit, ELCON said in comments.

“RTOs have been established or are forming in most parts of the U.S. and Canada, but the boundaries of these organizations do not always align with the boundaries of the local regional councils,” according to ELCON Executive Director John Anderson.

ELCON recommended that as more RTOs become operational -- and provided that NERC is rechartered with legislative authority to enforce compliance with its reliability standards -- the 10 current regional councils should be phased out and replaced with three interconnection-wide regional councils. Some reliability
If Competition Has Died, When Did It Live?

As a corporate energy manager, my job is to keep track of where energy markets are going. Accordingly, I was intrigued by recent reports that several CEOs from investor-owned utilities had decreed that the future of competition in electricity markets is dead. My first reaction was to recall Mark Twain's comment when he read his own obituary in a newspaper and said that "reports of this death are somewhat exaggerated."

From what I read, there was some discussion at a recent utility industry conference, with one CEO stating that "power deregulation was a failure" and that those who had predicted that "consumers would benefit from competition" were now proved wrong. Several other CEOs voiced agreement. Although at the same time, an industry spokesman for the Edison Electric Institute claimed that the industry as a whole still supported "restructuring."

That got me to thinking -- do deregulation, restructuring, and competition all mean the same thing? If not, what are the differences? And how do these differences affect what is happening in electricity markets?

I hear people use the three terms interchangeably. But I think they mean three different things.

To me, deregulation means taking an industry subject to heavy government regulation and removing all or most of that regulation. We may be able to deregulate the generation portion of the industry. But when it comes to "deregulating" the electricity industry, in order to make the transmission grid open and non-discriminatory, it may, in fact, require even more regulation.

Restructuring simply means a changing of rules, which can take many different forms. It seems obvious that changing the rules will result in an industry that operates differently. But despite somebody's best intentions, restructuring doesn't always result in an industry that is more efficient. And it doesn't necessarily mean that it will provide more benefits for consumers -- or for producers. It may just mean different winners and losers.

And then there's competition. Competition is -- or at least it should be -- the basis of our American economy. Competition is what makes free markets free. Competition is supposed to provide market efficiency, technology and innovation, and lower prices.

I am not an economist by training and I am not exactly sure how to define competition. But, as the old phrase goes, I know it when I see it. And, perhaps more importantly, in looking for competition in the electric utility industry, I know it when I don't see it.

Many states approved what they thought -- or at least what they claimed -- were plans for retail competition in the electricity industry. In truth, those states may have approved some degree of deregulation. They certainly approved a degree of restructuring. But it was the rare state that approved any changes that actually produced competition.

One reason is obvious: politics. When state legislatures debate electricity issues, the incumbent utilities are always among the loudest voices. Given their financial resources and their ability to communicate with consumers through the messages inserted in our monthly bills, it is no wonder that all too often state "competition" plans mirrored -- or almost mirrored -- anti-competition proposals put forth by

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The Chairman's View

It was a rare state that...actually produced competition.

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Competition Delayed, Not Dead, Anderson Tells Australian Group

The U.S. experience with electricity competition has shown what not to do, but we are still learning what the right things are to do, ELCON Executive Director John Anderson told the Australian Energy User Conference in Brisbane, Australia, recently.

Anderson was invited to give the perspective of American industrial electricity users on electricity markets in the United States. His address was entitled "Where is U.S. Electricity Policy Headed?"

He described how the regulatory structure that historically existed in U.S. electricity markets was flawed, keeping customers captive to utilities that had a wide range of rates.

"To some degree, the ability of an American manufacturing facility to be competitive in international markets depended on the luck of the draw -- where the facility was located and which utility provided power," he said. "And, utilities had no incentive to lower their rates or to seek lower cost power where it was available."

Beginning in the mid-1980s, he said, ELCON members saw the benefits of large, seamless, non-discriminatory markets with standard rules for all consumers. "We believed -- in fact we still believe -- that 'real' competition would bring lower prices, technological innovation, new products and services, a customer focus and the control of risk," he said.

Unfortunately, retail competition in the U.S. proceeded on a state-by-state basis, with about half of the states undertaking efforts to "restructure," and most experiencing disappointing results. "The market collapse in California, at least in part due to the gaming potential inherent in the California plan, fed the assertion that competition could not work," Anderson said. "The demise of Enron, which was really an accounting scandal, was also perceived as demonstrating the
Fate of Energy Bill Still Uncertain

It ain't over 'til it's over, baseball great Yogi Berra supposedly said. He might well have been describing the fate of the energy bill in Congress.

A comprehensive energy bill passed the House and Senate last year. A conference committee produced a compromise bill that was approved by the House but came up two votes short of the 60 needed to invoke cloture in the Senate. Without cloture, the bill's opponents were able to keep the measure from reaching a vote under Senate procedure.

While the electricity title of the bill is most important to ELCON, most of the controversy -- and opposition -- in the Senate centered on other provisions, including a liability waiver for manufacturers of the gasoline additive MTBE and $27 billion in tax breaks.

From ELCON's perspective, the electricity title of the conference report had some favorable provisions, including retention of the guaranteed purchase and sale provisions of the Public Utility Regulatory Policies Act (PURPA), which are essential to cogenerators, and a procedure to expedite siting of transmission lines to overcome local opposition. It also included several unfavorable provisions, including repeal of the Public Utility Holding Company Act (PUHCA), mandated participant funding for new transmission, “protection” for native load customers and, ELCON believes, unnecessary incentives for the construction of new transmission.

There have been numerous maneuvers to (1) redraft the comprehensive bill to make it “passable” -- i.e., get 60 votes, in the Senate -- and (2) take some provisions out of the energy bill and put them in other measures. For example, many of the tax provisions were added to the foreign tax bill in the Senate (not in the House) and will be considered as part of that legislation in an upcoming conference committee (though it is far from certain that either that tax bill or the energy provisions will actually be enacted into law). For a number of reasons, including the increased partisan rhetoric of an election year, the effort to redraft a comprehensive bill and bring it to the Senate floor did not make progress.

But despite the general observation that the comprehensive energy bill is “dead,” there are still several means -- albeit none necessarily likely -- by which some or all of the energy provisions could be enacted during this Congress.

The big unknown is whether Congress will return after Election Day for a lame duck session. Some Members have been saying that several issues -- including energy -- will be pushed into the November-December time frame. But the leadership in both houses insists that no decision has been made on whether to reconvene. If Congress does so, those Members trying to bring up a comprehensive energy bill hope for a less partisan session. Congress also could consider some components of the comprehensive energy bill on a piecemeal basis during the session between Labor Day and the election.

Democrats are trying to get Congress to consider the reliability section of the comprehensive bill's electricity title as a stand-alone measure. Rep. John Dingell (D-MI), senior Democrat on the House Energy and Commerce Committee, has undertaken a procedural effort to bring such a bill directly to the House floor. Sen. Maria Cantwell (D-WA) has taken a similar step in the Senate. Progress in either house will require cooperation from the Republican leadership, and that is not considered likely.

Nevertheless, these and other options remain possible. And until the 108th Congress actually adjourns, the energy bill remains -- just barely -- alive. E

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ELCON Works to Retain PURPA Guarantees

As the comprehensive energy bill proceeded in fits and starts through the 108th Congress (see related story this page), ELCON was successful in keeping certain guarantees in the Public Utility Regulatory Policies Act (PURPA) that are essential to cogenerators. Many ELCON members generate on-site with Qualifying Facilities (QFs) under PURPA.

At the beginning of this Congress, “conventional wisdom” held that well-funded utilities formally organized as the PURPA Reform Group had the votes to repeal PURPA provisions guaranteeing cogenerators the right to sell to utilities and to obtain back-up power at just and reasonable rates when necessary. Several utilities had sought for years to end those guarantees.

ELCON participated actively in a coalition of cogenerators along with representatives from the paper, chemical and steel industries; natural gas suppliers, and renewable and independent power producers to retain the provisions.

After months of negotiations, and through the good works of Representatives Rick Boucher (D-VA) and Chip Pickering (R-MS) and Senators Tom Carper (D-DE), Susan Collins (R-ME), Lamar Alexander (R-TN) and Mary Landrieu (D-LA), the conference committee on the energy bill agreed to keep the PURPA guarantees until competitive retail and wholesale power markets are established.

If the energy bill gets enacted this year, that favorable language will be included. If not, the even more favorable language in present law will be retained, and the starting point for debate next year will be the new “compromise.”

“The combined heat and power community -- industrial cogenerators, renewable energy, and independent power -- banded together on this one,” said Marc Yacker, ELCON's director of government and public affairs. "The utilities thought they had the PURPA issue won, but at the end of the day, strong lobbying and common sense prevailed." E
the utilities. For example, the now infamous California plan (AB 1890), which was flawed from day one, was primarily authored by Southern California Edison.

Competition should not include government mandated price caps, government established power exchanges, the imposition of stranded cost recovery on consumers or, most importantly, the continuation of utilities that can and do exercise market power derived from their government-granted monopoly status.

Competition in the electricity industry should include a direct and reasonably short transition from a market of vertically integrated monopolies to a market of free choice.

To me, intuitively, competition must include multiple buyers and sellers. In any electricity market there are almost always multiple buyers. The largest are the so-called Commercial and Industrial (C&I) customers, including large and small businesses. Many of these large buyers want to be able to purchase some of their power via long-term contracts for at least one year and sometimes longer if possible.

Electricity competition -- real competition -- can and should also benefit residential customers. These customers buy electricity in smaller quantity than the C&I folks, but they can often find lower prices by aggregating. That was one rationale for the creation, years ago, of public power (including both municipal and co-operative utilities), and that same reason is driving residential customers to form newly aggregated groups in some states right now.

Unfortunately, the "seller" part of the equation is all too often lacking in electricity markets today. Although about 20 states have enacted some form of electricity restructuring, in most states I am familiar with there are just not enough alternative suppliers to make competition work. My home state of Texas is one of the few (and maybe the only) exception, in that its competition plan established specific threshold levels of the market that must be served by new suppliers.

When retail competition was first discussed 10 or so years ago, I envisioned new, entrepreneurial companies serving as marketers or brokers, buying power from generators (both utilities and independent power producers) and then reselling that power to large and small customers at a (hopefully small) profit. By searching for the most efficiently produced electricity, marketers would enable customers to buy at a lower price. And their very presence would encourage the generation of low-cost power (as well as encourage innovation to produce even lower-cost power), thus providing benefits to all consumers, even those in so called low-cost states. In contrast, under the monopoly, guaranteed-
for our legal system.

“Everybody knows a basic premise of American jurisprudence is that no one is above the law,” said Anderson. “But apparently some utilities think that some laws don’t apply to them.

“The largest vertically integrated utilities want it both ways,” he asserted. “They should not be able to benefit from competition in wholesale markets by having the ability to sell uncommitted capacity at market-based rates, and yet, at the same time, exercise market power, raising the specter that the utility may stifle competition in its own backyard. It is consumers who end up paying higher prices.”

If the utilities don’t like FERC’s test for market power, they should seek judicial redress, not ignore the market power screens, according to ELCON.

“Utilities can seek a stay to delay implementation of FERC’s order,” Anderson explained, “but unless and until a stay is obtained, each of these utilities must comply with FERC’s Order.

“We agree with FERC’s statement that ‘market-based authority is not a right,’” he stated, quoting the April 14 order. “The Commission may grant such authority under the Federal Power Act only to applicants who demonstrably lack market power. This is a basic consumer protection.” E

Three Cases

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will presume that generation market power does not exist, but intervenors will be allowed to present contrary evidence.

Failing either screen will be presumed to show that generation market power exists, requiring the applicant either to produce additional evidence showing otherwise or to take mitigation measures, such as accepting cost-based rates or other steps to eliminate their ability to exercise market power.

ELCON urged FERC to begin to implement the new screens without delay, emphasizing that when the Commission authorizes market-based rates, it has a continuing duty to ensure that the relevant market remains sufficiently competitive to prevent unjust and unreasonable prices. If FERC gets the markets right, market-based rates in a competitive market should be the same or lower than cost-of-service rates.

AEP applied the market power screens to various control areas. It failed the market share analysis in its home control area in the AEP-SPP market and in the AEP-East control area (without integration in PJM). AEP claimed the failure reflected a problem with the screens in that they produce false negatives for vertically-integrated utilities. ELCON recommended in comments that as long as AEP-East remains on track for membership in PJM and fully complies with Order 2000, the Commission need not initiate a Section 206 investigation.

But, ELCON urged FERC to initiate an immediate investigation with respect to the AEP-SPP area, where plans for an RTO remain uncertain. The mere promise to participate in or join an ISO or RTO should not be grounds for delay, ELCON said.

Entergy applied the FERC screens to a number of control areas. It failed the market share analysis in its own control area (EES), but passed all others. Like AEP, it claimed the tests are flawed and tend to produce false negatives for vertically-integrated utilities. Entergy asserted that FERC should use other analyses to screen for market power.

ELCON member Occidental Chemical Corporation filed a motion, which ELCON supported in a separate filing, asking FERC to direct Entergy to provide data proving that other screens work better, and it urged FERC to investigate whether Entergy should continue to have market-based rates.

Southern Company applied six sets of screens to its markets -- the two from FERC and four others developed by its own consultant. Southern failed the market share analysis when applied to its own control area but passed its own screens. Alabama Electric Cooperative (AEC) asked FERC to reject Southern's report as "a non-compliant departure from, or arguments against, the market power screens adopted by the Commission...." ELCON filed a motion supporting AEC and asking FERC to investigate immediately whether Southern should be allowed to continue to have market-based rate authority.

NYISO Demand Curve

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power that is neither cost-based nor market-based. The price is not known until all generation is bid into a monthly “spot market auction.” The NYISO defended its proposal as necessary to stimulate new generation in New York and to encourage the continued operation of low-capacity generating units.

The industrials’ petition argues that FERC acted in an “arbitrary and capricious” manner in approving the NYISO petition on grounds that it will give more money to existing generators. There is no evidence that such profits will be translated into new capacity, the petition said. By approving the proposal, FERC failed in its responsibility to “relate its action to the primary aim of the Federal Power Act to guard the consumer against excessive rates.” The justification offered by NYISO and accepted by FERC does not meet that standard, the petition said.

“Keeping the system up and running is of paramount importance to industrial users,” Anderson said. “If the system is short of power at times of peak demand, residential consumers may lose their air conditioning, but industrial customers can lose their business.”

The Federal Power Act has a number of consumer protection features, Anderson said. “We are hopeful that the Court of Appeals will look at FERC’s approval of the NYISO Demand Curve and measure it against FERC’s responsibilities under the FPA,” he said. E
ISO-NE Demand Curve

The Federal Energy Regulatory Commission delayed implementation of the New England ISO's locational ICAP (LICAP) market until the conclusion of a hearing before an Administrative Law Judge concerning the parameters of the demand curve and capacity transfer limits. But, FERC agreed with the ISO's proposed use of a demand curve.

FERC rejected a proposed transition mechanism for creating unhedgeable costs and directed ISO-NE to submit a further filing on the issue of whether an additional ICAP region should be created for Southwest Connecticut.

ELCON has argued that the administratively determined demand curve in the proposal should be replaced with a real, market-determined demand curve. Price-responsive demand bids should be allowed to compete in all bid-based markets that any other resource provider -- such as a generator -- is allowed to bid.

FERC also had expressed continued concern about the advisory role of the members committee and required SPP explicitly to provide that absence of a members committee or regional state committee representative at a board meeting would not prevent the board from voting or making binding decisions. SPP agreed with these conditions in its most recent filing.

FERC had also found SPP's filing deficient in failing to provide a report clearly identifying transmission facilities under its control, which SPP provided in the followup filing.

Other issues that remain hanging include failure to adopt NERC classifications of service functions and failure to state clearly the responsibilities under each category. Nor has SPP demonstrated yet that it has acquired the authority to exercise day-to-day control over transmission facilities.

SPP revised its membership agreement and bylaws subject to proper formatting and designation of the tariff sheets, and FERC found that it satisfied the requirement for an independent board of directors. ELCON had pressed for establishment of an independent board, balanced stakeholder participation on the members committee, and a seams agreement with MISO.

MISO Tariff Conditionally Approved

FERC conditionally approved a MISO tariff that agreed with recommendations made by ELCON and other industrials by integrating demand response directly into the energy markets and creating a role for demand response resources (DRRs) to provide emergency capacity. MISO was directed to clarify what “price verification” of DRR offers above the $1,000
safety-net level would entail; to provide further detail on how it intends to measure DRR and what actions it would take for non-compliance, and to explain why DRRs should not participate in the reliability assessment process, serve as a capacity resource, or provide operating reserves.

FERC expressed some concern about whether MISO is indeed ready to implement the energy markets. It directed MISO to explain how it plans to ensure that the transition in functional responsibilities will not adversely impact reliability and to certify the reliability and readiness of the systems to FERC 30 days before market start-up. MISO must file a plan for full operational reversion to reliable system operations and transmission scheduling in the event of a serious system failure.

The RTO was also asked to clarify the division of reliability functions between itself and the control areas.

FERC approved implementation of LMP with a marginal loss component, as MISO proposed, but required MISO either to devise specific remedies for particular regions that may find themselves disproportionately exposed to marginal loss charges, or to modify the method for returning surplus charges to “loss pools.”

The proposed independent market monitor will be sufficiently independent to be able to monitor the Midwest markets, and the IMM’s oversight combined with application of the new interim generation market power screens will suffice to prevent the exercise of market power, FERC concluded. However, the Commission found the market monitoring proposal deficient with respect to the market monitor’s enforcement authorization.

Regarding seams issues, FERC instructed MISO to file a status report within 60 days, though it found that the lack of seams agreements would not prevent market start-up.

The treatment of grandfathered agreements (GFAs) is not resolved in the order, although FERC stated it would use best efforts to issue an order on GFAs as soon as possible. E

LMP Shortcomings Identified in S&P Report

A recent report from Standard & Poors highlights some of the shortcomings of locational marginal pricing (LMP). The report, "Makeover for California’s Power Markets," asserts that "though LMP does provide an economic signal, it's not immediately clear how the economic signal will translate into actual assets on the ground." The report also points out what industrial users have long thought was obvious - that generators may well realize that it is to their advantage not to alleviate congestion by building new facilities.

Industrial electricity users have long criticized the use of LMP as a means of easing grid congestion. Evidence shows that LMP does not, in fact, relieve congestion, and it adjusts prices on a nodal basis, resulting in unequal prices as well as price adjustments that were not in the tariff or contract.

"ELCON members, especially those operating in the PJM area which has used LMP for years, have long claimed that LMP is not the solution to the congestion problem," said ELCON Executive Director John Anderson. "It’s nice to have Standard & Poors saying the same thing." E

Pat Wood to Speak at ELCON Workshop

FERC Chairman Patrick Henry Wood III will be the headline speaker at ELCON’s Fall Workshop in October in Washington. The workshop, entitled "Where Do We Go From Here," is open only to ELCON members and attorneys representing state industrial user groups.

Chairman Wood has met with ELCON members on a regular basis in recent years. ELCON members have communicated to the chairman their support for pro-competition proposals including large, independent regional transmission organizations, mandatory mitigation measures to counter market power abuse, and uniform tariffs. At the same time, ELCON members have voiced dissatisfaction with several FERC initiatives, including the Commission’s frequent advocacy of locational marginal pricing.

Other speakers at the workshop will be Don Santa, president of the Interstate Natural Gas Association of America; Roy Thilly of Wisconsin Public Power; and Sharon Bonelli of Fitch Ratings. ELCON holds three workshops for members only per year. E

Competition Delayed

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shortcomings of competition."

Anderson outlined how competition has worked in several states, notably California, Pennsylvania, Ohio and Texas. He praised some features of the plan in Ohio, especially the ability to aggregate, and he noted that the Texas plan saved consumers over $1.5 million in 2002.

But, by and large, he said "states have been scared away from competition, either because of failures elsewhere or because of opposition from incumbent utilities and turf-conscious regulators."

Nevertheless, Anderson remained optimistic for the long term. "Over 52,000 MW of load has switched suppliers. The need for competitively priced electricity is as great as ever, particularly for manufacturers facing global competition. Competition is better than regulation when structured ‘correctly.’ We have learned what NOT to do. Unfortunately, we are still learning what we should do. It takes a long time to change a large industry. But that industry is broken. And it will be fixed." E
WHAT IS ELCON?

• DATE ORGANIZED: January 15, 1976

• WHO WE ARE: The Electricity Consumers Resource Council (ELCON) is the national association representing large industrial consumers of electricity. ELCON was organized to promote the development of coordinated and rational federal and state policies that will assure an adequate, reliable and efficient supply of electricity for all users at competitive prices. ELCON’s member companies come from virtually every segment of the manufacturing community.

• MEMBER COMPANIES: A.E. Staley Manufacturing Company • Air Liquide • Anheuser-Busch Companies, Inc. • BOC Gases • BP • Bunge Corp. • ChevronTexaco • Colonial Pipeline Company • DaimlerChrysler • Delphi Automotive Systems • E.I. du Pont de Nemours & Co. • Eastman Chemical Company • ExxonMobil Power and Gas Services, Inc. • Ford Motor Company • General Motors Corporation • Honda • Honeywell • Intel Corporation • MG Industries • Monsanto Co. • Occidental Chemical • Praxair • Procter & Gamble • Shell Oil Products • Smurfit Stone Container Corp. • Solutia, Inc. • Weyerhaeuser

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