

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Preventing Undue Discrimination and)
Preference in Transmission Services) Docket No. RM05-25-000

**STATEMENT
OF
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ON BEHALF OF
THE AMERICAN WIND ENERGY ASSOCIATION (“AWEA”)**

Order No. 888 Tariff Needs Major Overhaul

I. Introduction

My name is William L. Massey. I am a partner at Covington & Burling in Washington, DC. I served as a Commissioner at the Federal Energy Regulatory Commission from May 1993 until December 2003. Before that, I served as Chief Counsel and Legislative Director for Senator Dale Bumpers of Arkansas. I have a J.D. from the University of Arkansas School of Law and a Masters of Law from Georgetown University Law Center.

As I will explain in greater detail, and based on my extensive experience as a federal regulator and policymaker, it is my opinion that the Order No. 888 tariff is long overdue for a major overhaul. Simply tinkering at the edges will not solve today's serious problems related to grid balkanization, transmission pricing, congestion management, planning, discrimination in grid access, and market foreclosure of competitors. These issues must be addressed now if we are to avail ourselves of the enormous economic efficiencies and environmental benefits available from our abundant renewable resources, resources that are being artificially precluded from market access under the current open-access tariff regime. Critical tariff changes would also facilitate more reliable regional grid operation in a market environment. A timid approach will not achieve the Commission's often-stated goal of non-discriminatory grid access and robust wholesale markets. I am not suggesting a resurrection of Standard Market Design. Rather, I am saying that given the reality of the slow RTO development, we cannot escape the need to address, through bold modifications, the fundamental problems with the inadequate rules in effect today.

Years ago, the Commission crossed the great divide between cost of service regulation of wholesale electricity sales, on the one hand, and wholesale electricity markets

on the other. The movement to wholesale markets has been underway for well over a decade. The Commission has extensive experience with the Order No. 888 tariff and understands its weaknesses and inadequacies.

In EPCA 2005, Congress reaffirmed the nation's steady direction toward more competitive wholesale electricity markets - both with respect to transportation and sales. There are numerous provisions designed to expand the transmission infrastructure to further facilitate competitive markets (section 1241 regarding incentive-based rates and section 1263 repealing the Public Utility Holding Company Act of 1935) and additional regulatory tools to enable competitive markets to work better (enhanced market manipulation, transparency, and civil and criminal penalty authority). In addition, Congress did not disturb the Commission's deliberate and well-publicized movement toward market-based rates for sales of energy, capacity, and ancillary services.

After almost a decade operating under Order No. 888 and in light of the new energy law, the Commission has an obligation to ensure that its rules provide the framework for wholesale markets that function efficiently and reliably.¹ Anything less is contrary to FERC's legal obligations and not in the public interest.

II. Order No. 888 was right for the 1990s

Sections 211 and 212 of the Federal Power Act, initially enacted in 1978, expressly authorized the Commission to process petitions for electric transmission access

¹ As the Commission declared in the Notice of Inquiry, "The Federal Energy Regulatory Commission (Commission) has a mandate under sections 205 and 206 of the Federal Power Act (FPA) to ensure that, with respect to any transmission in interstate commerce or any sale of electric energy for resale in interstate commerce by a public utility, no person is subject to any undue prejudice or disadvantage. Under these sections, the Commission must determine whether any rule, regulation, practice, or contract affecting rates for such transmission or sale for resale is unduly discriminatory or preferential, and we must disapprove any of the foregoing that do not meet this standard." Notice of Inquiry at P 1.

on a case by case basis. Even as strengthened by amendments in 1992, that process was excruciatingly slow, with plenty of opportunities for the transmitting utility to litigate key issues and otherwise to delay grid access. Because the statutory provisions provided for an extensive process, the few cases instituted under Sections 211 and 212 moved glacially, and applicants simply were not getting access. The movement to open the grid so that customers could choose alternate suppliers seemed stymied. This did not seem to be what Congress intended.

The Commission decided to break the open access logjam with a generic approach patterned in many ways after Order No. 636, the landmark 1992 open access rule for natural gas pipelines. Orders No. 888² and 889³ were bold strokes at the right time. The orders required 167 jurisdictional transmission owners to take four fundamental steps among others: first, file a standard open access transmission tariff with non-discriminatory terms and conditions; second, provide transmission service separately from generation service; third, require the transmission owners' own wholesale generation function to take service under the open access tariff just like all other grid users; and fourth, post all relevant transmission system information such as capacity available for service, and process all service requests, on an Internet-based electronic bulletin board that is available to everyone.

² Order No. 888, Promoting Wholesale Competition Through Open Access Nondiscriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, FERC Stats. & Regs. ¶ 31,036 (1996) (Order No. 888), *order on reh'g*, Order No. 888-A, FERC Stats. & Regs. ¶ 31,048 (1997), *order on reh'g*, Order No. 888-B, 81 FERC ¶ 61,248 (1997), *order on reh'g*, Order No. 888-C, 82 FERC ¶ 61,046 (1998), *aff'd in relevant part sub nom*, Transmission Access Policy Study Group v. FERC, 225 F.3d 667 (D.C. Cir. 2000), *aff'd sub nom*, New York v. FERC, 535 U.S. 1 (2002).

³ Order No. 889, Open Access Same-Time Information System and Standards of Conduct, FERC Stats. and Regs. ¶ 31,035 (1996).

The Commission's early open access policies, coupled with the requirements of the Public Utility Regulatory Policies Act of 1978 with respect to cogeneration and renewable resources, provided the catalyst for sweeping changes in the U.S. electricity industry. Users of the grid multiplied as electric marketers and merchant generators entered the market. Within a few years, there were hundreds of wholesale electricity sellers in the U.S. New entry by merchant generators flourished.⁴

Order No. 888 firmly established the principles of open access, comparable transmission treatment for independently-owned resources, and competition in wholesale electricity markets. The comparability standard for transmission services resonated politically. It was essentially a variation of the Golden Rule -- transmission owners, you must do for others what you do for yourself.

While the goals and legal foundation for Order No. 888 were difficult to dispute, the rule's technical features were known to be imperfect. The Commission heard at the time from engineers and economists that the "contract-path" model used in Order No. 888 was a fiction that would eventually fail.⁵ Since the order and tariff provisions did not apply to bundled retail transmission used to serve the transmission provider's own native load, there was concern that tariff service would be inferior.⁶

⁴ Paul L. Joskow, "The Difficult Transition to Competitive Electric Markets in the U.S.," 16, Table 3 (the percentage of total electricity supplied by "non-utility" power suppliers increased from 10.7% to 33.6% from 1996-2002) (May 2003); Electric Power Supply Association, "Buy or Build? Power Purchases or Power Plant Ownership: Making the Best Choice for Customers," 1 (July 2004). ("competitive generators and combined heat and power generators have added approximately 160,000 megawatts of generating capacity in the United States since 1997").

⁵ Order No. 888, FERC Stats. & Regs. ¶ 31,036 (1996), 61 Fed. Reg. 21,540, 21,559 (May 10, 1996), (noting comments received in the Order No. 888 rulemaking on the contract-path basis for pricing and contracting).

⁶ *Id.* at 21,541 and 21,574-75.

During the same time frame, the Commission considered whether to adopt instead the “Capacity Reservation Tariff,” which would have put all customers on the same service and more appropriately respected the physics of real-time grid operation. The Commission decided, however, that a gradual phasing in of better practices over time would work best.⁷ Thus, the Commission’s pro forma tariff implemented the contract path approach rather than the capacity reservation approach, so that the concept of open access could be firmly established and the industry could begin its transition to the new world. Nevertheless, the Order No. 888 tariff was never intended to be immutable, but rather was intended to evolve over time as the industry changed, best practices emerged, and the Commission’s understanding drawn from market oversight deepened and became more sophisticated.⁸

Through an appellate process that culminated with review by the Supreme Court, the courts affirmed the Commission’s authority to adopt the new rules.⁹ Utilities began to separate their merchant and transmission functions. These legal and business changes along with the cultural changes and habits that accompanied them firmly established competition as the centerpiece of the wholesale electricity sector.

⁷ *Id.* at 21,573-75 (discussing capacity reservation issues in the Order 888 rulemaking); Capacity Reservation Open Access Transmission Tariffs, Notice of Proposed Rulemaking, Docket No. RM96-11-000, FERC Stats. & Regs. ¶ 32,519 (1996), *proceeding terminated*, 108 FERC ¶ 61,095 (2004).

⁸ For example, after a number of years of implementing Order No. 888, the Commission decided to standardize certain generator interconnection agreements and procedures. Order No. 2003, Standardization of Generator Interconnection Agreements and Procedures, FERC Stats. & Regs. ¶ 31,146, 30,523-24 (2003) (many decisions under the OATT are “subjective” and “a [t]ransmission [p]rovider that is not an independent entity has the ability and the incentive to exploit this subjectivity to its own advantage.”).

⁹ Order No. 888, *supra* n.2.

III. A tariff for robust regional markets is right for the 2000s

In the months and early years after implementation, the Commission came to the conclusion that additional restructuring was necessary to capture regional efficiencies and eliminate undue discrimination. In Order No. 2000, the Commission strongly encouraged transmission providers to form Regional Transmission Organizations (RTOs).¹⁰ It seemed obvious to the Commission even then that wholesale power markets were not utility-by-utility, or even state-by-state, markets. Instead, such markets were emerging regionally. The contract path was well understood to be a fiction, and contract path transmission pricing was inefficient -- grid users paid so-called pancaked rates as they moved power across several corporate boundaries. There still appeared to be bias in transmission access determinations, and efficient independent generators could not get dispatched.¹¹ Sensitive to political realities, the Commission encouraged, but did not require, the formation of RTOs to solve these problems. And a number of RTO/ISOs formed. There are now nine RTO/ISO entities in North America, including two in Canada.¹²

RTO/ISOs provide an independent platform for grid and market operations. They have efficient pricing. They eliminate pancaked rates. They generally have implemented a rational system of congestion pricing known as locational marginal pricing (LMP), moving away from the anachronism of contract path pricing that bears no

¹⁰ Order No. 2000, Regional Transmission Organizations, FERC Stats. & Regs. ¶ 31,089 (1999), 65 Fed. Reg. 809 (Jan. 6, 2000) (Order No. 2000), *order on reh'g*, Order No. 2000-A, FERC Stats. & Regs. ¶ 31,092, *aff'd sub nom*, Pub. Util. Dist. No. 1 v. FERC, 272 F.3d 607 (D.C. Cir. 2001).

¹¹ Order No. 2000, 65 Fed. Reg. at 817-25 (discussing the existence of “barriers and impediments” to achieving fully competitive electricity markets).

¹² These are ISO-New England, New York ISO, PJM, Midwest ISO, Southwest Power Pool, California ISO, ERCOT, Alberta Electric System Operator, and the Independent Electric System Operator (Ontario).

resemblance to actual power system dynamics and essentially ignores congestion to the grid. Most RTO/ISOs also implemented daily and hourly spot markets administered by an independent entity. In other words, the RTO/ISOs tackled dual problems -- not only grid access but also market foreclosure. All suppliers have the opportunity to bid into the markets without discrimination. In contrast to dispatch decisions under the Order No. 888 tariff, dispatch decisions within RTO/ISOs are transparent - RTOs implemented bid-based economic dispatch.¹³

All of these features -- regional planning and dispatch, independent grid and market operation, greater transparency, efficient pricing and locational price signals -- are clear and meaningful improvements over the Order No. 888 model.

But RTOs did not form in every region of the United States. In the wake of the California market failure, where an idiosyncratic market design produced poor results, the Commission attempted to standardize wholesale market design.¹⁴ The Commission proposed an RTO with certain common features and market elements for every region of the country. It is my view that the proposed standard market design was not defeated on the merits. If the goal is the elimination of undue discrimination and the establishment of efficient and robust wholesale markets, no one has proposed a better model. Industry and political representatives in certain regions of the country, however, strongly resisted

¹³ “The problem of insufficient and inconsistent data on transmission infrastructure, grid operations and market transactions has been documented by sources including the Energy Information and the Edison Electric Institute.” Report by the ISO/RTO Council, “The Value of Independent Regional Operators,” (ISO/RTO Council Report), 10, n.3. (November 2005).

¹⁴ Remediating Undue Discrimination through Open Access Transmission Service and Standard Market Design, Notice of Proposed Rulemaking, Docket No. RM01-12-000, FERC Stats. & Regs. ¶ 32, 563 (July 31, 2002) (SMD NOPR).

Standard Market Design. They mounted an effective political campaign, and the proposal was defeated politically.

As a result, the Commission is now faced with rather dramatic regional differences in the structure of wholesale electricity markets. The Commission has terminated the proposed SMD. Roughly two thirds of Americans live in regions served by RTO/ISOs and in 2004, RTO/ISOs delivered about 62 percent of the electricity consumed in the U.S.,¹⁵ with the rest under the Order No. 888 tariff with all of its known deficiencies.

Are these different treatments justified by real regional differences that the Commission must respect, or is there the need for rational pricing, more independent grid and market operation, regional planning and transparency, and greater standardization of market features such as Available Transfer Capability (ATC) everywhere? After all, the electric current that flows over the Eastern Interconnection in all directions at once at the speed of light is subject to different wholesale market rules as it flows through the Southeast than when it flows through the Northeast. In the Western Interconnection, the same electric current is subject to different market rules in California than in the Pacific Northwest. In my view, this situation is neither sustainable nor, from a policy perspective, desirable.

Given that the Commission's statutory obligations are national rather than regional, one could persuasively argue that there should be only one national policy for wholesale electricity markets and interstate transmission. Yet, we seem to be faced with a stubborn political reality. Some regions have not embraced Commission policy with respect to RTOs, and it appears to be current Commission policy not to force the issue.

¹⁵ ISO/RTO Council Report at 9.

And so, many have begun to ask, are there alternative ways to move effectively toward the ideal of independent grid operation and dispatch, grid regionalization, efficient pricing and market-friendly tariffs in the non-RTO regions? Can the Commission take significant, even bold, steps toward fairer access and dispatch decisions and more robust markets in regions that do not have, and perhaps will not have, RTOs? Outside of the RTO regions, can the Commission take the bold step of amending the Order No. 888 tariff to replicate in creative ways the most pro-competitive features of RTO/ISOs?

IV. Problems the Commission must address

A. Discriminatory grid access and dispatch

We now know that mere functional unbundling under the existing Order No. 888 tariff does not eliminate opportunities for discriminatory grid access decisions. In the Notice of Inquiry in this proceeding and in other orders, the Commission has referred to numerous ways in which non-independent transmission providers can exercise transmission market power, including delays and discrimination in honoring service requests, scheduling advantages, imbalance resolution, CBM manipulation, OASIS postings and calculation of ATC.¹⁶ It is simply axiomatic that in a market environment, these decisions must be made without bias. And importantly, various distinguished panels and task force reports focusing on reliability have also concluded that independence is essential. In 1997, the NERC Electric Reliability Panel concluded that the “operator must be independent from market

¹⁶ Notice of Inquiry at P 5; *see, e.g.*, Tucson Electric Power Co., 109 FERC ¶ 61,272 (2004); Entergy Servs. Inc., 109 FERC ¶ 61,281 (2004); *see also* SMD NOPR, *supra* n.14, 67 Fed. Reg. 55,452, 55,459-62 (discussing specific instances of undue discrimination and impediments to competition).

participants.”¹⁷ The Reliability Task Force, in its 1998 Final Report, concluded that entities with reliability authority must be independent of commercial interests “so that their reliability actions are -- and are seen to be -- unbiased and untainted”¹⁸

The theme of independent grid operation permeates Commission decision making going back for over half a decade. It is nothing less than foundational. If the Commission does not intend to amend the tariff to require grid access determinations that are fully independent of market participants, the Commission must find creative ways to move forcefully in this direction. Eliminating opportunities for discriminatory grid access is the cornerstone of well functioning markets.

In addition, Order No. 888 simply does not deal with the critical problem of foreclosing non-utility suppliers from dispatch. Non-discriminatory wholesale access to the grid, while essential, does not solve the related yet separate problem of discriminatory wholesale market access. Customers in wholesale markets must have access to the lowest cost generation available, not just utility generation. The RTO/ISOs solved this problem by allowing all resources to bid into the wholesale market without discrimination, and dispatch decisions are fully transparent. In stark contrast, if efficient and economic independent generators are blocked from access to the wholesale market, they cannot get dispatched even if they have secured access to the grid under Order No. 888. Customers simply do not have access to them. The Commission must amend the tariff to deal with this vexing issue. The tariff must implement a dispatch protocol that takes into account not just generation supply

¹⁷ Elec. Reliability Panel, N. Am. Reliability Council, *Reliable Power: Renewing the North American Electric Reliability Oversight System* 17 (Dec. 22, 1997).

¹⁸ Task Force on Elec. Sys. Reliability, U.S. Dep’t of Energy, *Maintaining Reliability in a Competitive U.S. Electricity Industry: Final Report of the Task Force on Electric System Reliability*, at xv (1998), *available at* <http://www.seab.energy.gov/publications/esrfinal.pdf> .

that is affiliated with the transmission provider, but all available resources on the system. Solving the problem of discriminatory market access goes hand in hand with solving the problem of discriminatory grid access.¹⁹

B. Tension between wholesale and retail transmission service

Ever since the Order No. 888 tariff was implemented, there has been considerable tension between wholesale and retail transmission services. Outside the RTO/ISOs, wholesale service and unbundled retail service are provided pursuant to a FERC tariff, while bundled retail service is provided pursuant to state rules. The Commission has often expressed the concern that two sets of access rules provide a fertile field for undue discrimination in access decisions. Subjecting all transmission uses to the same terms and conditions is the most logical solution. This action would help to eliminate opportunities for discrimination. Though politically challenging, moving boldly toward solving this fundamental problem is essential. This is not an issue that the Commission has the luxury of ignoring if its goal is nondiscriminatory grid access.

C. The U.S. electric grid remains balkanized and inefficient

Engineering and economics cannot be ignored by policymakers. Inefficient operations emerged soon after Order No. 888. Contract path transmission leads to underutilization of the grid and artificial congestion.²⁰ Scheduling protocols under the Order No. 888 tariff, outside the RTO/ISOs, are overly rigid and prevent efficient transactions from taking place.

¹⁹ *Supra* n.1.

²⁰ Sally Hunt, *Making Competition Work in Electricity* (2002) (Hunt), 147, 153-55. (discussing contract path transmission and congestion management).

Order No. 888 ignores the reality that wholesale power markets are regional. It embraces the fiction that they are state-by-state, utility-by-utility, control area-by-control area markets. It assumes that the markets respect control area, utility and state boundaries. These assumptions do not square with reality. NERC reports that there are currently 130 control areas in North America: 33 are in areas served by ISO/RTOs and the remaining 97 serve the rest of the country.²¹ Outside of the RTO/ISOs, transmission is scheduled conservatively to avoid loop flow affecting other transactions, with the result that the grid is substantially underutilized.²² Demand for transmission service has vastly expanded from ten years ago, so the strain caused by contract path scheduling is now much greater. In many cases, zero ATC is posted, yet physical capacity is available in all but 50 hours per year or less.²³

Remarkably, there are still pancaked rates under the tariff, years after the Commission sought to eliminate this gross inefficiency in Order No. 2000. Charges often in the range of \$3 to \$5/MWh are assessed in every corporate transmission boundary a transaction crosses -- even though the marginal cost of such transactions is a small fraction of such charges. Such barriers to trade limit the geographic scope of markets, discourage entry, and reduce options for customers.²⁴ The Commission must move away from the contract path, state-by-state, utility-by-utility fictions.

²¹ ISO/RTO Council Report at 14.

²² Hunt at 147; U.S. Department of Energy, "GRID 2030" A National Vision for Electricity's Second 100 Years, 7 (July 2003) ("The national average load factor ... is about 55%").

²³ Rocky Mountain Area Transmission Study Phase I Report, 5-10.

²⁴ "The impact of eliminating rate pancaking has been substantial," ISO/RTO Council Report at 21-22 (citing examples in MISO, NYISO, ISO-New England, and CAISO).

Balkanized control area by control area markets cry out for greater consolidation of control functions. In a 2002 filing before the Commission, NERC asserted that “RTOs with a regional perspective will do a better job maintaining system reliability than currently exists with multiple individual control areas over large geographic areas.”²⁵ Indeed, the Blackout Report found that a contributing cause in many large blackouts is poor communications among adjacent system operators.²⁶ This problem could be solved in part by a system operator with firm operational control²⁷ over an area for which real-time communication is essential for reliable operations.²⁸ In addition, it is particularly important for reliability purposes that a single grid manager have within its scope facilities that encompass a highly integrated and interdependent region.²⁹ Such a manager can see potential problems, and take corrective action in real time, over a broad area to prevent an impending cascade.

²⁵ Filing by NERC in Alliance Companies, Docket Nos. EL02-65-000 and RT01-88-016 (July 15, 2002).

²⁶ United States-Canada Power System Outage Task Force, Final Report on the August 14, 2003 Blackout in the United States and Canada: Causes and Recommendation (Apr. 2004) *available at* <http://www.electricity.doe.gov> (Blackout Report) , at 109, (“A common factor in several of the events described above was that information about outages occurring in one system was not provided to neighboring systems.”)

²⁷ At the time, MISO did not have firm real time operational control over the region it serves. *See* NERC Steering Group, N. Am. Elec. Reliability Council, Technical Analysis of the August 14, 2003, Blackout: What Happened, Why, and What Did We Learn?, 97 (July 13, 2004), *available at* <http://www.nerc.com/~filez/blackout.html>.

²⁸ “We understand that there have been instances where transmission system reliability was jeopardized due to the lack of adequate real-time communication between separate transmission operators in times of system emergencies. To the extent possible, RTO boundaries should encompass areas for which real-time communication is critical, and unified operation is preferred.” Order No. 2000 at 31,084.

²⁹ “To promote reliability and efficiency, portions of the transmission grid that are highly integrated and interdependent should not be divided into separate RTOs. One RTO operating the integrated facilities can better manage the grid.” *Id.*

The Blackout Report expressed concern about institutional fragmentation and decentralization of control and cited the operational inconsistencies and inefficiencies that arise from such fragmentation.³⁰ This problem could be solved, and reliability enhanced, with the merger of control functions into a system operator with control over a much broader and more rationally configured region.

It should be a national policy to consolidate smaller, less well equipped control areas into larger and regional, and more independent, state-of-the-art control centers. If the Commission does not intend to require or strongly encourage transmission providers to form or join transmission organizations, it should seek to replicate the virtues of such institutions by modifying the Order No. 888 tariff to eliminate pancaked transmission rates, replace contract path pricing with more efficient access charges, and require regional planning. It should use any available legal authorities to consolidate small control areas into larger regional institutions to facilitate more effective regional coordination and communication and better reliability. If it does not take this step, it should at least provide customers with the opportunity to dynamically schedule their energy into neighboring control areas, in order to prevent control areas that are too small from serving as a barrier to entry. This is particularly important for wind energy in the West.

³⁰ “Some observers believe that some U.S. regions have too many control areas performing one or more of the four critical reliability functions. In many cases, these entities exist to retain commercial advantages associated with some of these functions. The resulting institutional fragmentation and decentralization of control leads to a higher number of operating contacts and seams, complex coordination requirements, misalignment of control areas with other electrical boundaries and/or operating hierarchies, inconsistent practices and tools, and increased compliance monitoring requirements. These consequences hamper the efficiency and reliability of grid operations. . . . Moreover, it is not clear that small control areas are financially able to provide the facilities and services needed to perform control area functions at the level needed to maintain reliability.” Blackout Report at 146.

D. Physical bilateral markets do not lead to efficient dispatch

Physical bilateral markets pursuant to the Order No. 888 tariff, operated on a control area by control area basis, are inefficient.³¹ The Commission must insist on reaching the goal of larger, better coordinated regional markets outside of the RTO/ISOs.

In RTO markets, sellers need not always reserve capacity in advance. They can modify delivery as load fluctuates, weather changes, output changes, and as market opportunities arise. This is the way efficient markets work. All schedules are accepted with very few exceptions. Grid capacity is fully released to the market, and market prices allocate that capacity.

In contrast, a system of grid access and dispatch based solely on physical bilateral markets under the existing Order No. 888 tariff imposes significant transaction costs and achieves efficient utilization only if, by pure stroke of luck or divine intervention, hundreds of separate entities happen to schedule a set of transactions on the network that turns out to be the most efficient set in real time.³² This almost never happens. The physical contract path is not relevant to real time dispatch and reliability. Unanticipated equipment outages, significant weather changes, power transactions elsewhere on the network, and a host of other events that take place after forward markets close, often require a substantial modification to dispatch decisions if the required matching of supply and demand in real time is to occur and reliability is to be maintained. It also distorts market decisions because contracting parties whose grid usages create congestion do not pay the congestion costs they impose on the market. And in physical bilateral markets, so-called transmission loading

³¹ Hunt at 153.

³² See William Hogan, "Contract Networks for Electric Power Transmission," 4 Journal of Regulatory Economics, 411 (1992) (discussing merits of markets based on pools rather than bilateral contracts); Hunt at 285-98.

relief (TLR) occurrences displace transactions that do not match the realities of real time dispatch.³³

The deficiencies and problems outlined above will be even more pronounced as the generation mix changes over time. The next round of generation investment is likely to be more distant from load. Congestion and strains on the grid will only get worse.

Efficient congestion pricing can solve these problems. The Commission should amend the tariff to include a system of market-based congestion pricing. The ideal of course would be for such a system to be administered by an independent regional grid manager. If the Commission is able to structure such a system on a regional basis even in the absence of such an institution, it should do so. As an alternative, performance metrics should be placed upon any transmission provider that does not offer the ability to “buy through” congestion with locational pricing, such that any capacity that is found to be unused after posting zero ATC should trigger the obligation of the transmission provider to file new services to make this capacity available.

V. Robust regional markets promote state and federal renewable energy goals

With global climate change concerns increasing, the politics of global warming may be shifting in the U.S. Congress. Carbon constraints are being debated and even imposed by a number of states and regions. These changes, coupled with the skyrocketing price of oil and natural gas, have created an emerging and strengthening national policy consensus for promoting renewable energy.

Outdated electric industry rules, however, pose a significant barrier to renewable energy development. Wind energy in particular is growing 25 percent a year, and

³³ Hunt at 293-98.

the nation has the opportunity to benefit enormously through cleaner air, more domestic jobs, and energy security by exploiting our endless domestic wind resources. The cost of producing electricity from wind has decreased steadily and wind is now competitive in many areas. But barriers remain, the most significant of which is a balkanized and inefficient grid where opportunities for discrimination with respect to grid access and market foreclosure have not been eliminated.

Wind's intermittency is relatively easy to accommodate in robust regional markets within the RTO/ISOs. The cost of balancing the system when wind output varies is simply the cost of finding the cheapest unit across the large system to ramp up or down. That cost is small compared to the cost in small control areas. Most renewable resources have weather-driven output, and we would be better served with large regional markets that can readily accommodate these valuable resources.

Over the past few years, the Commission has moved steadily to implement policies that respect the special needs -- and recognize the enormous potential public benefits -- of wind and other intermittent resources. These actions are to be applauded. Nevertheless, the Commission's policies will not realize the full potential for wind unless Order No. 888 is subject to a major overhaul.

VI. The Commission should act boldly

The Commission should amend the Order No. 888 tariff to solve these problems. It is my opinion that large independent regional grid managers are the ideal. If, however, the Commission is not in a position to establish such institutions in all regions, it should seek to capture the benefits of such institutions through significant tariff reform.

The existing Order No. 888 rules were fine for the 1990s, but robust regional markets are essential for the 2000s. The Commission must address the dual but related

problems of discriminatory grid access and market foreclosure. It must eliminate discrimination between wholesale and retail service. It must correct the problem of grid balkanization and inefficient pricing and operations. It must move away from contract path pricing, pancaked transmission rates, and scheduling based upon a physical bilateral model. It should implement market-based congestion management on a regional basis. In short, if the Commission does not intend to regionalize the grid, it should adopt tariff rules to ensure that the grid works as if it were regionally coordinated. Our nation's electricity customers deserve no less.

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