

Monday, October 20, 2003  
Dual Plenary Session 11:00am-12:30 pm

Energy Trade and Transportation: Forward or Reverse?

Energy Trade and Transportation : Forward or Reverse? From the FERC  
Perspective

I am excited to appear on this panel and thank you for the invitation. Originally FERC Commissioner Nora Mead Brownell was to address this group but, as it turns out, she has a conflicting obligation. This morning Commissioner Brownell, together with Chairman Wood and Commissioner Massey, are presiding over a technical conference for the New York Independent System Operator (NYISO) in New York City. That technical conference is one in a series of regional technical conferences announced in the Commission's White Paper issued in Docket No. RM01-12-000 on April 28, 2003. The Commission is using these conferences to discuss with states and market participants in each region reasonable timetables for addressing wholesale market design issues and ways to tailor the final rule to benefit customers within the region.

I say this because the subject of my talk today is the Commission's actions to move energy trade and transportation forward. I would like to focus now on three Commission initiatives: 1) restructuring wholesale electricity markets; 2) improving efficiency in processing applications for pipeline and hydroelectric projects; and 3) increasing market monitoring. I also have a brief slide show of matters directly related to cross-border issues.

#### 1. Restructuring Wholesale Electricity Markets

The FERC has been working actively to restructure the wholesale electricity sector into the vibrant, competitive marketplace that customers deserve. The process began over six years ago when the Commission, in Order No. 888, ordered open access transmission. The process has been guided by five core principles:

First, customers must benefit. Restructuring markets toward a competitive outcome should be a value-added proposition. We are not abandoning what works, we are trying to make it better. In trying to make it better the Commission has undertaken a massive outreach effort to work with customers, state commissions and all market participants.

Second, the FERC must ensure independent operation of the nation's transmission highway. Such independence is essential to meeting Congress' directive in the Federal Power Act of nondiscriminatory access to the interstate grid. In Order No. 2000, the Commission identified the benefits of large, independent regional entities, or RTOs, in operating the nation's transmission grid.

Third, the FERC must promote the development of a robust and reliable infrastructure that supports the dispatch of generation on a least-cost basis. Until all wholesale generators can compete fairly on an economic basis, customers will continue to be deprived of potential savings.

Fourth, the FERC must ensure transparency in the electricity markets. Clear rules of the road are necessary to attract capital for infrastructure investment. A market cannot run efficiently unless the rules are clear and there is adequate opportunity for price discovery. We can't assume this without an independent system operator and full access to information.

Fifth, the FERC must ensure adequate customer protection against unjust and unreasonable rates. This begins with a well-functioning wholesale electricity market and also requires vigilant market monitoring at all times and mitigation whenever appropriate. It also means that the appropriate regulator or market monitor addresses and resolves expeditiously any market problems that arise so the industry can move forward.

Let me rattle off a list of recent Commission initiatives which advance the development of energy markets. These recent Commission initiatives relate directly to the five (5) principles I just listed.

1. Modifications to our affiliate rule and a new policy statement on price indices for both gas and electric industries,
2. Increased staffing in the Office of Market Oversight and Investigations,
3. Issuance of Order No. 2001 requiring detailed reporting on transactions and the filing of quarterly accounting reports,
4. Development of standardized procedures for interconnection of generators greater than 20MW, and a NOPR for small generator interconnection,
5. Aggressive investigation of the causes of the Western energy crisis, and
6. Issuance of proposed "market behavior rules" which call for all electric market based rate tariffs and gas blanket certificates to contain provisions relating to: (1) market manipulation, (2) communications, (3) reporting and (4) record retention. Sellers violating the new rules would be subject to

disgorgement of unjust profits and other non-monetary remedies including revocation of market based rate authority.

These are just a few examples of recent Commission actions in furtherance of these five principles.

However, the single most important initiative the Commission has been pursuing is the creation of Regional Transmission Organizations (RTOs). The Commission views this as the single most effective way of achieving these five goals simultaneously.

RTOs that are fully independent of market participants can ensure nondiscriminatory operation of the transmission facilities under their control.

RTOs

- have FERC-approved market monitors,
- implement FERC-approved market mitigation plans,
- conduct long-range planning all for the protection of customers,
- can perform economic dispatch over large geographic areas that will ensure the selection of least-cost generators, and, finally,
- can offer organized markets and one-stop shopping that reduce transaction costs, provide transparent market rules and allow the opportunity for price discovery.

I am pleased to report that the majority of public utilities now seem to recognize the value of RTOs – almost every transmission-owning public utility has announced its intention to join a specific RTO. The FERC has

- granted RTO status to the Midwest ISO and PJM Interconnection,
- granted conditional RTO status to several RTOs including West Connect and RTO West,
- has several other RTO filings pending, and
- expects RTO filings from several others in the near future.

The standard market design rulemaking and our White Paper have been an invaluable source of information as the FERC works through the RTO filings. The wealth of comments we have received on the proposed standard market design rule has given us a much greater understanding of how to create a commercial platform within RTOs that will ensure the maximum benefits for customers. Regional differences should and are being accommodated in RTOs. Nevertheless, market platforms must be consistent in order to ensure equity, eliminate barriers to entry,

reduce transaction costs, and create an environment where gaming is limited, if not eliminated. The platform must also ensure that the most appropriate solution, whether transmission, generation or demand-side, is implemented.

## 2. Improving Efficiency in Processing Energy Project Applications

The FERC has responsibility for authorizing the construction and operation of interstate natural gas pipelines and hydroelectric projects. Any entity that proposes to site, construct and operate or modify facilities used to import or export natural gas must file an application with FERC pursuant to Section 3 of the Natural Gas Act and file for the issuance of a Presidential Permit with the Department of Energy. We have been improving our processes for handling project applications so that our processes do not impede market development, and may in fact advance infrastructure.

Revisions to the pipeline certification processes have resulted in reduced processing time from an average of 273 days in 1995 to 195 days today. Since 2001, the FERC certificated more than 17 Bcf per day of new capacity.

More recently, the FERC, after hearing complaints for years about the inefficiency of the licensing process for hydroelectric projects, has proposed changes to the hydroelectric licensing regulations. Hydroelectric projects are a critical component of this nation's energy infrastructure, and inefficiencies in FERC's re-licensing process add unnecessary costs and uncertainties to the detriment of consumers. The proposed rule would create a new process in which the current duplicative, sequential environmental analyses conducted separately by the license applicant, the FERC, and the other agencies is replaced with a single "integrated" environmental analysis. We estimate that the proposed rule would reduce the average time it takes to complete the licensing process by 30 months—cutting down 47 months of preparation and processing time to 17 months. Further, we estimate that the proposed process would reduce the cost of licensing for a project of less than 5 megawatts by \$150,000 and for a project greater than 5 megawatts by \$690,000.

## 3. Market Monitoring

The FERC's other relatively recent initiative has been on market monitoring and

investigations. Much has been said over the historic failure of market monitoring and without revisiting history, I believe we now recognize that market monitoring must:

- Be the responsibility of everyone;
- Be a continuous proactive process anticipating trends, understanding market dynamics and inter-dependencies;
- Have dedicated resources;
- Develop effective ongoing communications with regional market monitors, state commissioners and Mexican and Canadian regulators;
- Clearly understand financial markets and customer needs;
- Co-ordinate effectively with sister agencies; and
- Analyze, inquire and investigate.

I am pleased to report that the Commission has made substantive changes in FERC's market monitoring with the reformation of the Office of Market Oversight and Investigation (OMOI). OMOI is charged with the above objectives and, with nearly a full staff complement, is well on its way toward meeting them. Similarly, FERC is working with the US-Canadian Joint Task Force to identify the cause of the Blackout on August 14, 2003 and devise co-operative solutions to prevent future transmission failures and promote reliability in wholesale power markets.

Slide Show:

Electric Cross Border  
Gas Cross Border Pipeline Projects  
LNG Proposals