

Report to Western Governors on an Enhanced Regional Electricity Function in the Western Interconnection June 2004

The causes and economic consequences of the 2000-2001 Western electricity crisis that began in California and rippled across the entire Western Interconnection are well-understood. The necessary steps to avoid a future crisis, however, are not in place. The Western industry is deeply divided about the value of Regional Transmission Organizations and the appropriate role of the only existing grid-wide institution, the voluntary Western Electricity Coordinating Council. Many are skeptical about the wisdom and feasibility of remedies advocated by the Federal Energy Regulatory Commission.

Since the crisis, Western governors have been the only effective unifying force for improving the operation of our interconnected Western electricity grid. Western governors provided the catalyst for improvements in transmission planning and permitting. They have recommended actions to protect the reliability of the grid and improve the assessment of the adequacy of resources to meet demand.

However, the bridge to a reliable and economic Western electricity system is fragile and in need of continuing gubernatorial attention. The next step in strengthening the Western electricity system requires an enhanced state and provincial regional electricity function that can help implement the governors' direction through sound analysis and active participation in grid management issues. In its current form, the existing Committee on Regional Electric Power Cooperation of the Western Interstate Energy Board's¹ is not capable of providing the necessary level of analysis and participation.

In December 2002, Western governors directed that the concept of an enhanced state/provincial regional electricity function be explored. In the fall and winter of 2003-2004, the Committee on Regional Electric Power Cooperation undertook a bottom-up evaluation of the value of an enhanced regional electricity function in five critical areas:

- Reliability;
- Resource adequacy;
- Market monitoring;

¹ The Western Interstate Energy Board includes all the states and provinces in the Western Interconnection. Its members are appointed by the governor or premier. Its legal basis is an interstate compact. The Board serves as the technical energy arm of the Western Governors' Association. The Board's Committee on Regional Electric Power Cooperation is comprised of interested state and provincial utility regulatory commissions, governors' energy agencies and facility siting agencies in the Western Interconnection. The Committee was established in 1984 and is a valuable forum for sharing information on issues affecting the Western grid. The Committee rarely adopts positions on issues. When it does it acts by unanimous agreement.

- Transmission planning and expansion; and
- Transmission permitting.

In March, the Committee consolidated the findings from work groups in each of the five areas into recommendations to Western governors. In brief, the Committee found:

- Continued progress in pro-active transmission planning is contingent on the voluntary efforts of a few companies and regular engagement of Governors; pro-active planning has not become routine.
- The WGA Transmission Permitting Protocol appears adequate for coordinating permitting reviews of proposed interstate transmission lines, but has not yet been tested because no new interstate transmission line has been proposed since the Protocol was signed in 2002.
- At this time, the West does not need the formality of an interstate compact, nor is there a need to transfer any state-level authority to a regional body.
- However, there is an urgent need to enhance the regional electricity function.
 - This requires additional resources for states/provinces to act regionally to:
 - Ensure quality analysis of the adequacy of resources to meet demand;
 - Enable coordination among the states/provinces and the Federal Energy Regulatory Commission on monitoring Western electricity markets;
 - Enable active state participation to advance regional transmission planning and expansion and ensure Governors' policy objectives are addressed.
 - To be successful, any enhanced regional electricity functions need the imprimatur of Western Governors.
 - Governors should establish a task force to examine options for sustainable funding of regional electricity functions.
 - Initial budget estimates range from \$800,000 to \$900,000 and cover: a small core staff and operating budget (\$435,000); funds to contract out technical work (\$250,000); and state/provincial travel funds (\$150,000). Further support may be necessary to respond to possible federal energy legislation containing provisions on reliability or preemption of state transmission siting and permitting authority. By comparison, the initial budget for an analogous group established in 2003 in the Midwest called the Organization of Midwest Independent System Operator States is slightly less than \$1 million per year.
- If federal energy legislation is enacted to establish mandatory reliability standards and grant the Federal Energy Regulatory Commission the power to pre-empt state electric transmission siting laws, then additional action is needed.

- Governors would need to create an interconnection-wide Regional Reliability Advisory Body.
- Additional resources would be needed to participate in the federal government's identification and designation of "national interest" transmission lines where state permitting authority would be pre-empted.

The Committee recommends that the Governors (1) accept the recommendations, (2) direct that a process be established to solicit stakeholder input on the recommendations, and (3) take action on the recommendations at the WGA 2004 winter meeting.

Absent political leadership of Western Governors backed by improved analysis and greater participation by state and provincial agencies, the West will not be prepared to deal with a future Western electricity crisis. That failure will set the stage for federally-imposed solutions that may not meet the needs of the region.

Attachments

- 1 Findings and Recommendations of the Committee on Regional Electric Power Cooperation
2. Chronology of Developments

Attachment 1

Enhancing Regional Electricity Functions in the Western Interconnection:

Findings and Recommendations of the Committee on Regional Electric Power Cooperation Adopted March 26, 2004

At its October 2003 meeting, the Committee on Regional Electric Power Cooperation launched a bottom-up evaluation of the value of a regional body that would be more formal than the Committee. This evaluation was done in response to a request by the Western Governors. The five work groups that were formed and the leaders of each are:

- a. Reliability – Bill Chamberlain
- b. Market Monitoring – Lou Ann Westerfield
- c. Resource Assessment/Adequacy – Grace Anderson
- d. Transmission Planning and Expansion – Steve Ellenbecker
- e. Transmission Permitting – John Savage

The workgroups were tasked with developing white papers on the current state of affairs in their respective topic areas and the value of a more formal electric decision making body.² The Regional Decision-Making Work Group was charged with synthesizing the information from the reports of the five other work groups and proposing recommendations for the Committee on Regional Electric Power Cooperation to consider making to Western Governors. The following sections contain highlights of the findings of the work groups and proposed recommendations of the Decision-Making Work Group.

Findings

Reliability. The existing state and provincial participation on the Board of Directors of the Western Electricity Coordinating Council provides a valuable avenue for representing the public interest in decisions of that voluntary organization. (Four of the 27 members of the Western Electricity Coordinating Council Board of Directors represent states and provinces.) If federal reliability legislation is enacted and compliance with reliability standards becomes mandatory and enforceable in the U.S. by the Federal Energy Regulatory Commission, there will be need for a body with representation from all states and provinces in the Western Interconnection to participate in the process of setting and enforcing standards. The pending federal reliability legislation includes provisions enabling governors to establish regional reliability advisory bodies to advise the Western Electricity Coordinating Council, a North American reliability organization, and the Federal Energy Regulatory Commission on reliability issues. Where such a body covers an entire interconnection, the Federal Energy Regulatory Commission may defer to the advice of such body. The legislation also contemplates the same funding vehicle for regional advisory bodies as would be used to fund the Western Electricity Coordinating

² The Work Group reports can be found at <http://www.westgov.org/wieb/electric/mse/REFwrkgrp/wrkgrps.htm> .

Attachment 1

Council and a North American reliability body. This, presumably, would be through fees collected by control area operators.

Market Monitoring. Western Governors and state commissions have a compelling need to ensure that market abuses are detected and mitigated. There is a need to expand and better coordinate state and provincial participation in market monitoring activities by FERC's Office of Market Oversight and Investigations and a West-wide market monitor, if one is established. This increased participation would include collective regional interaction with market monitors on an ongoing, routine basis and could extend to participation in decisions on the formation of a West-wide market monitor.

Fulfilling these needs will require the increased capability of states/provinces to meet in a timely manner, including emergency meetings. The degree of required coordination does not rise to the level of an interstate compact, but is more than presently provided by the Committee on Regional Electric Power Cooperation.

Resource Assessment/Adequacy and Transmission Planning/Expansion. The most pressing need is to improve or develop capabilities to ensure that needed analysis and communication occur among states/provinces and with Western grid organizations (e.g., the Western Electricity Coordinating Council, Seams Steering Group-Western Interconnection). Among the specific improvements urgently needed are:

- An energy (kilowatt-hour) assessment for the region, especially given the importance of hydro resources, natural gas supply limits, and energy limited sub-regions.
- Including the probability of severe but likely weather in regional assessments.
- Improving information on the adequacy of resources for specific load-serving entities (including municipal utilities and retail access providers) and sub-regions of the Western Interconnection.
- Identifying where responsibility for meeting load growth resides and should be strengthened.
- Linkage of regional electricity system adequacy analysis with natural gas availability, infrastructure and price information, as called for in a September, 2003, Western Governors' resolution.³
- Developing and agreeing to assessment metrics and adequacy targets/standards.
- Understanding the effects of price signals (for example for transmission access and congestion) and how they could be improved.

³ North American gas production is declining. The Seams Steering Group-Western Interconnection estimates indicate that in a likely future, gas-fired generation will be at least 40 percent of Western Interconnection capacity (nominal megawatts) and 27 percent of generation (megawatt-hours) for 2008. Gas shortages, particularly in a cold dry winter, could cause problems for reliability and wholesale prices.

Attachment 1

- Exploring actions which could prevent a potential return to the unacceptable conditions and repercussions of 2000-01.
- Understanding the transmission planning processes at various levels: interconnection-wide, in sub-regions/states/provinces, and at RTOs/transmission-owning companies.
- Integration of transmission and generation planning.

While states/provinces should not be obligated to address these shortcomings by themselves, it is imperative that they play a major role in the assessments and have the capacity to evaluate and convey the implications of such assessments to governors, premiers and regulatory bodies. The most pressing need in improving resource assessment/adequacy is to identify consistent funding sources to support the conceptual development and integration of analyses that will enable states/provinces to better execute their electricity policy and regulatory functions.

Transmission Permitting. Under the current legal structure, which does not preempt state transmission permitting authority, we find that the Transmission Permitting Protocol of the Western Governors' Association is likely to provide an adequate level of interstate coordination. However, we recognize that the Protocol has yet to be tested and experience may reveal some necessary modifications.

If Congress enacts legislation that provides for Department of Energy designation of "national interest transmission corridors," Federal Energy Regulatory Commission preemption of state siting and permitting authority in such corridors, and authority to the Western Area Power Administration to build "national interest" transmission lines, a more formal regional body of states/provinces will be needed. This could be in the form of an expanded WGA Protocol or, in the extreme, an interstate compact.

At this time, there is not a compelling demonstrated need to establish an interstate compact that would exercise the electricity decision-making authority that currently resides with the states. However, improvements are needed now to address the regional issues outlined above, and the scope and nature of the improvements should be revisited in the event federal energy legislation is enacted.

Recommendations

1. The analysis and communication capabilities of the Committee on Regional Electric Power Cooperation/Western Interstate Energy Board/Western Governors' Association should be significantly expanded in the area of resource assessment/adequacy. Immediately needed work products include:
 - (a) development, public review, and critique of a west-wide and sub-regional energy (kilowatt-hour) assessment;

Attachment 1

- (b) integration of natural gas availability and price assessment into electricity assessments; and,
- (c) review and critique of data and metrics, applied at appropriate sub-regional levels (such as the transmission constraint zones), that can provide meaningful assessments of adequacy.

The capability to produce such work products, or evaluate those developed by others, would be achieved through a combination of contracting, additional staff support, continued technical and coordination support from state/provincial staffs and members of the Western Electricity Coordinating Council and the Seams Steering Commission-Western Interconnection.

2. The analysis and communication capabilities of the Committee on Regional Electric Power Cooperation should be expanded in the area of transmission planning and expansion. States/provinces need to effectively participate in interconnection-wide and sub-regional transmission planning efforts on a sustained basis. They need to evaluate and integrate the results of these planning efforts in order to: (a) advise governors/premiers of the implications of ongoing transmission planning, (b) advise transmission planning processes of the recommendations of governors/premiers, and (c) improve reviews of the resource plans by their jurisdictional load serving entities.
3. If federal reliability legislation is enacted, Western Governors should establish a Western Regional Advisory Body to advise the Western Electricity Coordinating Council, the North American Electric Reliability Council, and the Federal Energy Regulatory Commission on reliability-related issues.
4. A state/provincial market monitoring group should be established, initially within the Committee on Regional Electric Power Cooperation, and charged with the task of collaborating with the Federal Energy Regulatory Commission's Office of Market Oversight and Investigations, and any West-wide market monitor that is created, in the sharing of information on market performance. The state/provincial market monitoring group would act as an intermediary between the Federal Energy Regulatory Commission and Governors' offices and state commissions. Each state/province would be invited to appoint a lead market monitoring representative to the group. Other state/provincial agency personnel could also participate. The group would be charged with maintaining regular interaction with the Office of Market Oversight and Investigations and any West-wide market monitor, and reporting to the Committee on Regional Electric Power Cooperation. The group needs to have the resources to hold meetings more frequently than the Committee on Regional Electric Power Cooperation and to meet on an emergency basis.
5. The resource analysis/adequacy, market monitoring, and transmission planning and expansion activities outlined above need to be conducted with the imprimatur

Attachment 1

of Western Governors and, if possible, Western Premiers. This could be achieved in several ways. In the absence of federal legislation, we recommend that Western Governors direct that the activities outlined above be undertaken and that there be periodic reports on these topics to the governors. If reliability legislation is enacted, we recommend that a Western Regional Advisory Body appointed by Governors be the point of accountability to Governors, and if possible, Western Premiers, for these functions. (Note that transmission permitting activities under the WGA Transmission Permitting Protocol already include a reporting requirement to Western Governors.)

6. If federal legislation is enacted authorizing the preemption of state transmission permitting functions, there should be an immediate reexamination of the need for a formal body to participate in Department of Energy designations of “national interest” corridors, the Federal Energy Regulatory Commission’s granting of eminent domain, and the Western Area Power Administration’s exercise of transmission construction authority.
7. The Committee on Regional Electric Power Cooperation should continue as a forum for sharing information among states and provinces in the Western Interconnection and engaging in discussions with the Western industry and the Federal Energy Regulatory Commission. However, as legislative and other changes occur and the above recommendations are implemented, the value of the Committee on Regional Electric Power Cooperation needs to be reassessed.
8. Western Governors should establish a working group to craft a system to provide sustainable funding for an enhanced regional electricity function in the Western Interconnection, as outlined in this document. The most pressing immediate needs are in the areas of resource assessment, transmission planning and market monitoring.

Attachment 2

Chronology of Developments

- Fall 2000 Western wholesale electricity prices reach record levels during normally slack demand period.
- December 2000 **Governors hold emergency meeting in Denver**
- No satisfactory answers to questions of why electricity and natural gas prices are at record levels.
 - Then-Energy Secretary Richardson orders all parties in West to supply electricity to California.
- February 2001 **Governors hold energy roundtable**
- Electric prices still at record levels, economic damage spreading beyond California.
 - FERC unsuccessful in mitigating prices.
 - Roundtable makes recommendations (which form basis of WGA Energy Policy Roadmap resolution).
- May 2001 **Governors hold transmission roundtable**
- No answer to governors' question of whether we have enough transmission.
 - Governors direct crash effort to develop a conceptual transmission plan for the Western Interconnection.
- August 2001 **WGA Annual meeting**
- Governors receive first conceptual transmission plan for the West.
 - Governors adopt Energy Policy Roadmap resolution asking
 - Industry to develop an ongoing proactive transmission planning process; and
 - Calling on Congress to enact legislation enabling enforcement of reliability standards.
 - Governors direct development of a protocol for collaboration of permitting agencies in the review of proposed interstate transmission lines.
- June 2002 **WGA Annual meeting**
- Governors attending sign WGA Transmission Permitting Protocol. By September 2002 all governors in the Western Interconnection and four federal agencies have signed the Protocol.

Attachment 2

- December 2002 **WGA Winter Meeting**
- **WGA lead governors for energy (Kitzhaber, Geringer) urge colleagues to establish a regional electricity entity to better enable governors and the region to avoid future crises.** See attached letter.
 - **Governors direct that the concept of a regional electricity entity be explored.**
- February 2003 Governor Richardson, WGA lead governor for energy, delivers to Governors a status report on plans to explore the value of a regional electricity entity.
- September 2003 WGA receives grant from DOE to explore regional electricity entity concept.
- September 2003 **WGA Annual Meeting in Big Sky**
- In wake of August power outage in the East, Western Governors adopt a resolution on electric reliability directing WGA staff to develop a plan to implement the Regional Reliability Advisory Body provisions of pending federal energy legislation (which remains stalled in Congress).
 - Governors add to the WGA Energy Policy Roadmap resolution a request to develop an assessment of the adequacy of electric (and related natural gas) resources to meet demand in the Western Interconnection.
- November 2003 **WIEB's Committee on Regional Electric Power Cooperation (CREPC) (all the states and provinces in the Western Interconnection) begins a bottom-up evaluation of value of a regional electricity entity.**
- Five key areas for review are identified:
 - Reliability;
 - Resource adequacy;
 - Market monitoring;
 - Transmission planning and expansion; and
 - Transmission permitting.
 - Work groups are created to examine five priority areas and whether a regional entity would add value.
- March 2004 **The Committee on Regional Electric Power Cooperation unanimously adopts recommendations to Governors to create an enhanced regional electricity function.**
- April 2004 **Stakeholders in two of the breakout sessions at the WGA**

Attachment 2

North American Energy Summit recommend an expanded role of states/provinces in Western grid issues.⁴

WGA Staff Council is briefed on the recommendations of the Committee on Regional Electric Power Cooperation.

⁴ A. Governors should create a formal regional state entity to:

- Work with FERC to address competitive western wholesale markets, while states retain decisions on retail access
- Ensure regional coordination on transmission planning/expansion
- Address financing of new transmission

B. Governors should establish a formal region wide policy group to assess issues and make recommendations to state decision makers on regional energy issues with a public funding commitment from each state, compositions might include existing state commissions.

Attachment 2



**WESTERN
GOVERNORS'
ASSOCIATION**

Judy Martz
Governor of Montana
Chairman

James M. Souby
Executive Director

Headquarters:
1515 Cleveland Place
Suite 200
Denver, Colorado 80202-5114

303-623-9378
Fax 303-534-7309

Washington, D.C. Office:
400 N. Capitol Street, N.W.
Suite 388
Washington, D.C. 20001

202-624-5402
Fax 202-624-7707

www.westgov.org

December 2, 2002

The Honorable Michael O. Leavitt
Governor of Utah
210 State Capitol
Salt Lake City, UT 84114

Dear Mike:

The Western governors have been engaged with the Administration and Congress on energy legislation for well over a year. We have been particularly concerned about the electricity title and its potentially negative effects on the Western Interconnection, which ties 11 of our states and parts of three others together into a common electric grid.

We expect the debate over the electricity title to resume early next year, and the region needs to be well prepared to engage in that debate and the longer-term struggle over implementation of electricity policy. Our experience over the past two years has shown that when Western governors have taken the initiative to engage Congress, the Federal Energy Regulatory Commission, and the Department of Energy on a sustained, substantive basis, we have been able to turn back intrusive federal policies and reshape federal decisions to meet the needs of the region.

As you know an energy bill was not enacted during the lame duck session. Therefore, we have a brief, post-election hiatus to assess the situation, review our options and plan for the new year. In addition, FERC jumped into the fray last year with its proposed Standard Market Design rule, a complicated proposal to create regional electricity markets, which many states believe would usurp part of a state's authority to regulate electricity. While FERC has extended the comment period on key elements of the SMD rule, such as market design in the Western Interconnection and state roles, we have only until January 10, 2003 to affect the outcome.

The debate has been vigorous and time consuming. The issues surrounding the regulation of electricity are complex; and, as we learned from California's experience, perverse consequences can arise from the best-intended decisions. We have been able to get a workable reliability provision into both the House and Senate bills, but we have been unable to influence provisions involving electricity market design in the legislation. The elections leave this matter up in the air. Therefore, it is prudent that we take steps to protect the interests of the region, including grid reliability, and expand our capability to implement Western solutions derived from the collaborative efforts of the states and Western industry.

The Honorable Michael O. Leavitt
December 2, 2002
Page 2

As the lead governors for energy issues, we recommend that the states in the Western Interconnection strengthen how we cooperate among ourselves and interact with the federal government and Congress. Throughout the electricity debate, we have relied on our staffs, our Public Utility Commissions and other public and private allies to advise us. The Committee on Regional Electric Power Cooperation (CREPC) has been particularly helpful. This voluntary committee of our PUCs and energy and facility siting advisors has provided important analysis and recommendations. These efforts have been coordinated by WGA and the Western Interstate Energy Board (WIEB). While this has been an effective way to engage Congress and stay abreast of the activities in Washington, D.C., our efforts have also illuminated some weaknesses that need to be shored up.

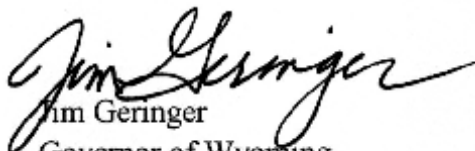
The weakness that concerns us is the lack of a more thorough and formal mechanism for the states in the Western Interconnection to manage interstate affairs and interact with FERC and the Administration on regulatory issues that affect the interstate grid. Given the complexity of these issues and the enormous consequences decisions will have on our economies and the well being of our citizens, we can no longer afford to deal with them on an ad hoc, voluntary manner. This will be particularly true if an SMD rule is adopted.

Our preference would be to strengthen the deliberations of a subset of state representatives within CREPC, including finding a stable, regional funding source to staff its operations, while ensuring accountability to governors. In this way, we would not be creating a new organization, but strengthening the body WGA, WIEB and the PUCs have come to rely on for advice and recommendations.

We have asked the staff at WGA and WIEB to analyze our recommendation, and they will be providing your staff council member with their analysis next week. We hope you will give this recommendation serious and favorable consideration at the Winter Meeting of WGA on December 6.

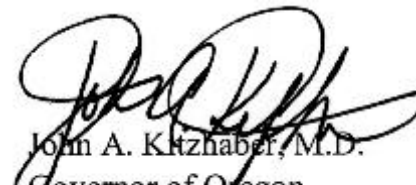
In the meantime, should you or your staff have questions or concerns, please contact Jim Souby or Doug Larson at 303-623-9378.

Sincerely,



Jim Geringer
Governor of Wyoming

Lead Governor for Energy



John A. Kitzhaber, M.D.
Governor of Oregon

Lead Governor for Energy

cc: Governor Frank Murkowski, Alaska
Governor Tauese Sunia, American Samoa
Governor Carl Gutierrez, Guam
Governor Linda Lingle, Hawaii
Governor Bill Graves, Kansas

Governor Mike Johanns, Nebraska
Governor John Hoeven, North Dakota
Governor William Janklow, South Dakota
Governor Rick Perry, Texas