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NORTH AMERICAN ELECTRIC RELIABILITY COUNCIL

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April 4, 2002

Hon. Jeff Bingaman, Chairman
Committee on Energy and Natural Resources
Room SD-364
United States Senate
Washington, D.C.

Reliability Legislation

Dear Chairman Bingaman:

The North American Electric Reliability Council (“NERC”) appreciates the leadership that you and Senator Frank Murkowski are providing toward completing work on a comprehensive energy bill in this session of Congress. As NERC has testified before the Senate Energy and Natural Resources Committee on several occasions, it is vital to the continued reliability of the North American high-voltage transmission system that we have in place a system of mandatory and enforceable reliability rules, applicable to all users, owners, and operators of the bulk electric system in North America. The bill now before the Senate, your amendment in the nature of a substitute to S. 517, as further amended by the Thomas amendment (No. 3012) to Section 207 (which the Senate adopted on March 14, 2002), meets that vital need. NERC urges the Senate to pass legislation including the Thomas amendment on reliability this year.

I regret that we have been unable to reach agreement with you on reliability legislation so far in this Congress, and truly hope that we can find such agreement now. To that end, I would like to respond to a number of the arguments made during the floor debate on the Thomas amendment.

Let me start with what the Thomas Amendment does. The Thomas amendment would authorize creation of a single industry-based electric reliability organization (“ERO”), whose mission would be to develop and enforce rules for the reliable operation of the high-voltage transmission system in North America, subject to oversight within the United States by the Federal Energy Regulatory Commission. Contrary to the impression created by the amendment’s critics, FERC’s role under the legislation is substantial:

- FERC will conduct a rulemaking to implement the legislation, and it will have the power to define terms, establish additional requirements, and otherwise influence the organization and activities of the ERO.
- FERC must authorize the ERO before it can begin operation and must approve its governance, procedural rules, and funding mechanism.
- FERC must approve any proposed changes in the ERO's governance, procedural rules, or funding mechanism and also has the power to direct changes to those items.
- No reliability standard developed by the ERO can take effect until FERC has first provided notice and an opportunity for comment and then issues an order permitting the reliability standard to take effect.
- FERC has the power to direct the ERO to change an existing or proposed reliability standard and to develop a new reliability standard where one does not exist.
- No enforcement action by the ERO can take effect until the proposed action is filed with FERC. FERC has the power to affirm, modify, or set the proposed enforcement action aside.
- FERC must approve any delegation of enforcement authority to a regional entity. FERC may take the actions it deems necessary to assure compliance with the statute and the Commission's rules by the ERO or any regional entity having delegated enforcement authority.
- Finally, FERC may rule on any complaint that a state's action with respect to the bulk power system is inconsistent with a reliability standard.

Much has been made by opponents of the provision in the Thomas amendment requiring FERC to remand a proposed reliability standard that it disapproves instead of specifying the appropriate reliability rule itself, as FERC does with the rates of public utilities. Two fundamental reasons support the remand requirement. First, the reliability rules are a complex set of interdependent technical standards governing a very complicated system. The industry has the technical experience and expertise to address those highly complex matters. FERC does not possess, and it is not likely to acquire, the necessary expertise any time soon. The requirement for a remand assures that any problem that FERC identifies with a proposed reliability standard can be properly addressed by those with the technical expertise to solve the problem and that FERC does not inadvertently require a change to a reliability standard that could jeopardize the reliability of the interconnected grid.

Second, the interconnected transmission grid is international in character. The Western Interconnection reaches from the Canadian provinces of British Columbia and Alberta, through the continental United States from the Rocky Mountains to the Pacific Coast, to a portion of Baja California Norte, Mexico. The Eastern Interconnection includes Canadian provinces running east from Saskatchewan to the Atlantic Coast and the rest of the continental United States outside the Electric Reliability Council of Texas. Finally, plans are under way to interconnect ERCOT with parts of the grid in the mainland of Mexico. International participation in the ERO allows for development of proposed reliability standards that satisfy regulators and interests in all jurisdictions. A remand to the ERO allows for changes to proposed reliability standards that also satisfy regulators in all jurisdictions, again because of international participation in that effort. If FERC itself modified a proposed reliability standard, it would be dictating the reliability rules to be followed in Canada and Mexico as well.

Some assailed the rebuttable presumption that the Thomas amendment affords a reliability standard proposed by an interconnection-wide regional entity that is to apply interconnection-wide. They questioned why standards proposed to apply on an interconnection-wide basis should be afforded a rebuttable presumption, while those proposed to apply just to one region within an interconnection should not. The rebuttable presumption for interconnection-wide reliability standards makes sense because an interconnection-wide standard, by its very nature, must take account of all the electrical consequences that may occur within that interconnection. Each of the three interconnections (Eastern, ERCOT, and Western) functions as a single, very large machine. There can be legitimate reasons why some standards should be different. ERCOT, for example, now operates as a single control area (load-generation balancing area) so not all of the electric reliability organization's reliability standards would apply as they do in the other two interconnections, which contain multiple control areas. In the Western Interconnection, for example, the use of power system stabilizers is more prevalent than in other interconnections, necessitating some different standards. In neither of these examples is reliability affected in another interconnection. On the other hand, if one or more regions or subregions *within* an interconnection followed different standards, there could be significant adverse reliability consequences to other regions or subregions within that interconnection, and also some significant inequities. That is not to say that there cannot be regional differences within an interconnection, only that they would not be entitled to a rebuttable presumption. Because differences in standards within an interconnection can have significant reliability implications throughout the interconnection, they must receive more scrutiny to make sure that such differences do not adversely affect the reliability of other parts of the same interconnection.

Even in the case of an interconnection-wide standard proposed by an interconnection-wide organization, however, the presumption that the standard is acceptable may be rebutted. If either the ERO or FERC determines that such a standard is unjust, unreasonable, unduly discriminatory or preferential, or not in the public interest, it may provide the basis for this determination and "rebut" the "rebuttable presumption." Once a rebuttable presumption is challenged, it no longer enjoys any special treatment or deference, and the matter would be decided on its merits.

Some argued that the Thomas amendment would impose improper restrictions on FERC's authority over regional transmission organizations. The amendment does no such thing. FERC retains full authority over RTOs. During the rulemaking that led to FERC's Order No. 2000, some organizations that hoped to become RTOs argued they should be able to set their own reliability rules. FERC rejected that argument and ruled that RTOs should follow the reliability standards set by NERC or its successor organization. Under the Thomas amendment, an RTO would be a user, owner, or operator of the bulk power system and thus subject to the reliability standards, just as is the case for all other bulk power system users, owners, and operators. FERC also said that if a reliability standard interfered with the RTO's ability to meet its responsibilities under Order No. 2000, the RTO should inform FERC. FERC's powers, as described above, would provide FERC ample authority to resolve any conflicts between the reliability standards and the RTO's responsibilities under FERC's rules.

Some pointed to the current industry discussions on establishing an organization to develop consensus wholesale electricity business practice standards and communications protocols as a reason not to adopt the Thomas reliability language. However, the electric reliability organization contemplated by the Thomas amendment is completely consistent with the creation of another organization to develop consensus business practice standards. On March 15, NERC filed comments with FERC strongly endorsing creation of a business practices organization, with NERC continuing to focus on reliability issues. NERC committed to coordinating the development of its reliability standards with the business practice standards activity and explained how that coordination would take place. If the industry failed to properly coordinate those efforts, FERC would be in a position to pass upon both the reliability standards and the business practice standards before either of them took effect, thus assuring that the two sets of standards would be compatible and consistent with the Commission's overall goals of promoting reliable and well-functioning competitive wholesale electricity markets. Many in the electric industry, including the American Public Power Association, Arizona Public Service Corporation, National Association of State Utility Consumer Advocates, National Rural Electric Cooperative Association, Southern Company Services, Inc., Transmission Access Policy Study Group, Western Area Power Administration, and Wisconsin Electric Power Company, joined in NERC's position. Other organizations, such as the National Association of Regulatory Utility Commissioners, echoed NERC's position in pleadings of their own.

Perhaps the most incredible claim made by opponents of the Thomas amendment is that in some unspecified way the reliability amendment would "interfere with the development of competitive wholesale markets." To the contrary, a clear set of mandatory and enforceable rules for the reliable operation of the bulk electric system provides the best foundation on which to develop competitive wholesale markets in electricity. All participants in the market must respect the physical limits of the interconnected system, and competition can then take place within those physical limits. This country has a very competitive airline industry, but it also has a Federal Aviation Administration that sets rules for aircraft separation in flight, the frequency and spacing of landings at airports, and the timing and scope of required airplane maintenance.

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Those fundamental FAA rules for the safety of airline passengers form the foundation on which competition within the airline industry can take place. The Congress should be wary of those who give lip service to reliability while supporting approaches that could undermine it — some of those to whom the rules would apply are arguing against an effective mechanism for adopting and enforcing the rules.

Finally, the argument was made that the Thomas amendment will require the creation of a complex, new bureaucracy. The truth is that the Thomas amendment builds on the existing bulk power system reliability mechanisms, albeit changing them to reflect new competitive market realities and the FERC oversight necessary to enable the new reliability organization to promulgate and enforce *mandatory* reliability standards. It is those who seek to replace these existing mechanisms with FERC that would require the creation of a new expertise and organization at FERC to do in the future what it has never done in the past.

In closing, let me again thank you for the leadership you are providing in moving an energy bill through the Senate. I would welcome the opportunity to meet with you and to discuss further how we can work together to maintain the reliability of the interconnected grid in North America.

Very truly yours,

A handwritten signature in black ink, appearing to read "Michael R. Gund", with a long horizontal flourish extending to the right.

cc: Senator Frank Murkowski
Senator Craig Thomas