

TO: State Energy Directors & NASEO Affiliates
FROM: Rich Sedano
SUBJECT: Electricity Reliability
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Electricity Reliability

As many of you probably know a major change is potentially taking place in how electricity reliability is being ensured in the United States. It is possible that a change being proposed would diminish the role of states in regulating reliability. This is a highly complex subject and the issue relates to how you define reliability and the nature of where state and federal jurisdiction begins and ends in an era of restructuring. This memorandum covers some current events, and is intended to provide an explanation as to why state energy offices should become more informed and involved. We will also be discussing this issue at the NASEO meeting next month in Washington, D.C.

At its own initiative, the North American Electric Reliability Council (NERC) is changing to the North American Electric Reliability Organization (NAERO). NERC was formed by the electric industry after the New York blackout of 1965. NERC developed reliability standards and grid operating protocols through a consensus process. NERC standards and protocols have been followed on a voluntary basis. NERC has been governed by a Board of Directors with membership limited to electric transmission owners. The overarching issue is, to what extent will NERC be transformed into a self-regulating reliability entity with authority to set reliability standards and enforce compliance with such standards. This will require federal legislation to vest reliability authority in the Federal Energy Regulatory Commission (FERC). Under this legislative scenario FERC would delegate certain functions and authority to NAERO, while retaining oversight. When NAERO is established the existing NERC Board of Directors will dissolve, to be replaced by a Board, composed of individuals with no financial interest in the electric power industry. In addition, on January 4, 1999, nine additional members (not part of the industry) were added to the existing 37 member Board. These new members apparently will become the entire NAERO Board after a transition period.

As part of a year long process instigated by NERC to develop consensus federal legislation on reliability, representatives of states have been included in a committee review. Representatives of the National Association of Regulatory Utility Commissioners (NARUC) and the National Association of State Utility Consumer Advocates (NASUCA) have participated in this process. The Department of Energy, through Bonnie Suchman of the General Counsel's office, has also been involved in this process. From the perspective of the states, within the past two weeks the process has broken down. Consideration had been given to ensuring a strong state role in regulating reliability. The consensus achieved (without the states) now eliminates any state role or oversight function in bulk power system reliability.

In concept, the results of this effort may now be included in the Administration's electric restructuring legislation, without a state role on reliability. The historical responsibilities of states exercised through their regulatory institutions would transfer to an industry organization with ultimate authority at the federal level in the form of FERC. State functions, such as determining the appropriate generation reserve margins, the acceptable level of system reliability and possibly approval of transmission investment and cost recovery from ratepayers would transfer to the industry/federal government structure being proposed. This has been especially troubling to the western states that have participated in a regional process that would preserve regional authority over reliability issues. This is also important because there will be an early effort to move a stand-alone electricity reliability bill in Congress. Some believe that if more comprehensive legislation will not move that a smaller effort could be successful. It should be noted however that if the states are not happy with the legislative proposal, this process could be stopped dead in its tracks.

I led a conference call recently on this subject with the NASEO representatives serving on the National

Council on Competition in the Electric Industry, including Bill Keese (CA), Pat Meier (WI), Fred Hoover (MD), as well as Frank Bishop and Jeff Genzer. The consensus was that this was a critical issue and that we should inform the states and discuss this matter to develop a unified position. We are working closely with NARUC and NASUCA, as well as other organizations on this subject.

In a related development, on November 24, 1998, the Federal Energy Regulatory Commission (FERC) initiated a process to consult with state utility commissions on the establishment of regional electric transmission organizations or districts. FERC's view appears to be that regional power markets must be facilitated by regional institutions such as regional transmission organizations or independent system operators. This has also been seen as a way to establish new reliability principles. There is concern among the states that certain groupings, either along the lines of existing power pools or Independent System Operators, might be inappropriate. The Western Interstate Energy Board recently wrote to FERC and asked that a broader representation of state interests be consulted with in the context of the discussion over transmission grids.

Hearings are scheduled for February 1999 in three locations across the Country: 1) February 11 - St. Louis; 2) February 12 – Las Vegas; and 3) February 17 - Washington, D.C.

A meeting is being planned for April 15-16 in Dallas, Texas, which is intended to bring together key stakeholders to discuss electricity reliability issues. Break-out sessions are presently planned among potential reliability district groupings. The meeting has three critical purposes: 1) to educate key federal and state policymakers on electricity reliability issues; 2) to develop policy consensus on reliability; and 3) to address the role of states individually and jointly in developing and implementing reliability policies and practices at the state, regional and national levels. EPRI is also considering developing a program immediately before the conference to discuss these matters on a technical basis.

I hope readers in state energy offices will find these reliability issues important. Suggestions on how NASEO can or should be acting in this area are welcome. For example, NASEO members could be actively involved in these fundamental changes to the power system. If you are interested we can provide you copies of the proposed legislation and you may wish to express your views to FERC in conjunction with the ongoing consultations, as well as to participate in the upcoming conference referenced above.