

**SUMMARY OF THE TESTIMONY OF DAVID K. OWENS
ON BEHALF OF THE EDISON ELECTRIC INSTITUTE
BEFORE THE COMMITTEE ON ENERGY AND COMMERCE
U.S. HOUSE OF REPRESENTATIVES
SEPTEMBER 4, 2003**

EEI will defer to the international investigative effort being led by DOE for the United States to provide answers to questions about specific factors and events leading up to and contributing to the recent blackout. Instead, we will focus on the policy issues raised by the recent power outages, especially those addressed in the pending energy bill.

- An electric reliability organization, with FERC oversight, should be created to develop and enforce mandatory reliability rules and standards that are binding on all electric companies and market participants. Reliability provisions are included in both the House and Senate versions of the pending energy legislation.
- FERC should be given limited backstop transmission siting authority to help site transmission lines in “interstate congestion areas” designated by DOE, if states have been unable to agree or move forward in a timely fashion. The House version of the pending energy bill includes this provision.
 - The transmission permitting process on federal lands should be reformed and simplified by designating DOE as the lead agency to coordinate and set deadlines for the federal environmental and permitting process. Deadlines for the designation of transmission corridors across federal lands should be established. The House version of the pending energy bill includes these provisions.
 - Repealing PUHCA will help attract the billions of dollars of new capital needed to increase investments in new transmission infrastructure and modernize the existing infrastructure using new technologies. Both versions of the energy bill include provisions to repeal PUHCA.
- FERC and the states should utilize innovative transmission pricing incentives, including performance-based rates and higher rates of return, to attract capital to fund needed investments in transmission. The House version of the pending energy legislation includes FERC pricing provisions.
- The U.S. tax code should be amended to provide enhanced accelerated depreciation (from 20 to 15 years) for electric transmission assets, similar to the tax treatment governing other major capital assets. In addition, Congress should ensure that electric companies that sell or otherwise dispose of their transmission assets into a FERC-approved regional transmission organization (RTO) or independent transmission company (ITC) do not suffer tax penalties. Accelerated depreciation provisions are included in the House version of the pending energy legislation; both the House and Senate versions of the bill address transmission sales or dispositions.

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Mr. Chairman and Members of the Committee:

My name is David K. Owens, and I am Executive Vice President of the Edison Electric Institute (EEI). EEI is the association of U.S. shareholder-owned electric utilities and industry affiliates and associates worldwide. We appreciate the opportunity to testify on the electric power outages that affected regions in the Eastern Interconnection for several days in August.

The Committee has requested information on the specific factors and events leading up to and contributing to the blackout. While there has been a great deal of speculation about the sequence of events that caused the blackout, we believe that the international investigative effort being led for the United States by the Department of Energy (DOE), with technical expertise from the North American Electric Reliability Council (NERC), the regional reliability councils and the affected regional transmission organizations (RTOs) and individual utilities, will provide answers to those questions.

Our testimony will focus on the policy issues that have been raised by the recent power outages, especially those addressed in the pending comprehensive energy bill, and what we believe Congress can do to help prevent similar incidents in the future.

Electricity Competition and the Infrastructure

The question of whether electricity competition caused the blackout has been repeatedly asked and argued about. We believe that is not the relevant question.

Competition in wholesale and a number of retail electricity markets exists, and we cannot retreat from these markets. We must work together to make competitive markets work.

Electrons follow the laws of physics. No matter what utility structure model exists – competitive, a mixed model or fully integrated – there must be adequate infrastructure in place and appropriate rules for reliable operation. Sufficient transmission capacity is a critical building block in all of the models. Without adequate transmission, none of the models will work.

The recent blackout, whatever its causes, reveals that the current system faces many stresses. Fortunately, Congress can help to relieve those stresses with a number of provisions that are included in the pending energy legislation.

Ensure Reliability Standards are Mandatory and Enforceable

NERC was formed in the aftermath of the 1965 power outages in the Northeast, and for more than thirty years, NERC has set voluntary reliability rules and standards. This system has generally worked well in the past, but today's electricity market requires a mandatory reliability system, with enforcement mechanisms. The number of market participants has increased dramatically, as have the number and complexity of electricity transactions being transmitted.

Since early 1999, a broad group of stakeholders, including EEI and many of its individual member companies, have supported legislation that would create an electric reliability organization, with Federal Energy Regulatory Commission (FERC) oversight, to develop and enforce mandatory reliability rules and standards that are binding on all electric companies and market participants. Reliability provisions supported by these stakeholders are included in both the House and Senate versions of the pending energy

legislation. We strongly urge inclusion of these reliability provisions in a final energy bill.

Remove Roadblocks to Transmission Investment

The level of investment in the long-distance, high-voltage wires has not kept pace with the growing demands being imposed on the system because of greater electricity use, competition in wholesale markets and related factors. Thus, it is not surprising that the transmission grid is becoming increasingly congested:

- According to NERC, the volume of actual transmission transactions has increased by 400 percent in the last four years. Transactions that could not be completed because of congestion on transmission lines increased five-fold to almost 1,500 in 2002, compared with 300 uncompleted transactions in 1998.
- Congestion in the Mid-Atlantic region, where the highly respected PJM RTO controls transmission, has quintupled between 1999 and 2001 to \$271 million, before increasing to \$430 million with the additional of PJM West.

Billions of dollars are being spent annually on new transmission facilities, but the bulk of the new transmission being built is to help serve local load and connect new generation to the grid. More emphasis is needed on removing disincentives to investment in the long-distance, high-voltage wires needed to strengthen regional electricity markets, such as siting delays, regulatory barriers and tax policies.

In the early 1970s, the annual growth rate in lower voltage line-miles that support localized grid operations and interconnections was 1.9 percent, while the annual growth rate for high-voltage line-miles was 3.2 percent. By the latter half of the 1990s, this

relationship had reversed: the higher voltage line-miles were growing at only 0.3 percent, while lower voltage line-miles were growing at 3.5 percent.

According to the Energy Information Administration (EIA), consumer demand for electricity is going to increase by roughly 50 percent over the next two decades. To meet this increase in demand, capital investments in upgrades and new transmission lines must increase from the current level of \$3 billion annually to roughly \$5.5 billion annually over the next ten years.

A number of critical disincentives actually discourage investment in transmission, including:

- Local opposition to siting new facilities,
- Inability to recover planning and related costs when facilities are delayed or ultimately rejected by siting authorities,
- State retail rate caps that may prevent utilities from recovering their investments in transmission,
- Uncertainty over transmission ownership and control policies, and
- Uncertainty as to whether beneficiaries will pay for new transmission.

Grant FERC Backstop Siting Authority

While traditional state siting processes will be adequate for most local upgrades to existing transmission systems, limited FERC backstop siting authority to help site new transmission lines in interstate congested areas would be a critical aid in developing the more significant transmission infrastructure needed to support regional wholesale electricity markets.

Before states will grant utilities siting permits, utilities typically must prove that the new facilities are needed. The determination of “need” often focuses on service to in-state consumers and not to consumers across an entire region. In fact, many state siting laws do not allow for the consideration of regional, or out of state, benefits of new transmission lines. If states consider only intrastate benefits and not regional benefits, they may have little choice under state law but to reject the proposed line, even if the benefits to the region are significant.

As competitive wholesale electricity markets continue to develop, multi-state RTOs will increasingly gain operational control of utility transmission lines. But, most state siting laws do not recognize the role new entities such as RTOs or independent transmission companies will play in transmission planning and siting. It is not clear that these new entities would even be considered utilities under state laws.

Regional electricity markets require a siting process that has the ability to consider regional and even national needs. FERC has jurisdiction over wholesale electricity markets, but, unlike its authority to site natural gas pipelines, it currently does not have any authority over transmission siting to help ensure that there is sufficient transmission capacity to support those markets.

The House version of the pending energy legislation gives FERC very limited backstop transmission siting authority. This authority extends only to helping site transmission lines in “interstate congestion areas” designated by DOE and only if states have been unable to agree or act within a year. We strongly urge its inclusion in the final version of the energy bill.

FERC has decades of experience in siting energy facilities. Since 1948, interstate natural gas pipelines have gone to FERC for certificates that grant them eminent domain authority. FERC has permitted hydroelectric facilities since 1920.

Protection of the environment is a top consideration in FERC's processing of natural gas pipeline certificates. Under the National Environmental Policy Act (NEPA), FERC is required to perform a comprehensive environmental analysis of all gas pipeline construction proposals. The House transmission siting provision would require the same environmental protection process for any transmission line construction proposal.

Reform the Federal Lands Permitting Process

The unnecessarily complicated, time-consuming and difficult multi-jurisdictional federal permitting process to site energy facilities, including authorizations for siting across federal lands, is another major impediment to building new transmission. In some areas of the country, this is the principal impediment.

Problems with the federal permitting process include (1) a severely fragmented process, where each federal agency with potential jurisdiction has its own set of rules, timelines for action and processes for permitting; (2) the tendency by federal agencies to require multiple and duplicative environmental reviews; (3) a failure to coordinate with any state siting process; and (4) a lack of harmonized permit terms from one agency to the next.

The federal transmission permitting process needs to be coordinated, simplified and made to work with any state siting process. The House-passed energy bill accomplishes this objective by designating DOE as the lead agency to coordinate and set deadlines for the federal environmental and permitting process. In addition, DOE would be

responsible for coordinating the federal process with any state and tribal process. A state where a transmission facility would be located could appeal to DOE when a federal decision deadline has been missed or a federal authorization has been denied. To further facilitate siting, the House version of the energy bill sets deadlines for the designation of transmission corridors across federal lands. We strongly support inclusion of these provisions, with some technical modifications, in the final energy bill.

Repeal the Public Utility Holding Company Act (PUHCA)

We also believe that repealing PUHCA will help attract significant amounts of new investment capital in the industry. By imposing limitations on investments in the regulated energy industry, PUHCA acts as a substantial impediment to new investment in energy infrastructure, keeping billions of dollars of new capital out of the industry. As a result, we believe that PUHCA has contributed to the failure of the electricity infrastructure to keep pace with growing electricity demand and the development of regional wholesale markets.

We also believe that repealing PUHCA will help expedite the formation of interstate transmission companies (ITCs). ITCs can play an important role in planning and building new transmission infrastructure. However, interstate transmission companies could be required to become registered holding companies and subject to PUHCA's restrictions and additional regulation, making it more difficult to raise financing.

Both House and Senate versions of the pending energy bill contain provisions that would repeal PUHCA and transfer consumer protections to FERC and the states. These provisions should be included in the final energy bill.

Reform FERC Transmission Rate Policies

We believe that FERC and the states should utilize innovative transmission pricing incentives, including performance-based rates and higher rates of return, to attract the capital necessary to fund needed investment in transmission. In addition, transmission users must pay their fair share of the system's costs. We support the FERC pricing and transmission technologies provisions in the House version of the pending energy bill. Likewise, we encourage the states to assure that utilities can recover their costs for investments for transmission under state regulation, with a reasonable rate of return.

According to a December 2001 FERC "Electric Transmission Constraint Study," transmission costs make up only 6 percent of the current average monthly electric bill for retail consumers. On the other hand, generation costs make up 74 percent of the average bill. By reducing transmission congestion, investments in new transmission will allow greater economic dispatch of lower cost generation.

FERC estimates that a \$12.6 billion increase in transmission investment would add only 87 cents to an electric customer's average monthly bill. But, since increased transmission investment will help reduce congestion and enable lower cost power to reach consumers more easily, FERC anticipates that the net benefits to overall electric bills could be potentially quite large.

For example, FERC estimates that if the reduced transmission congestion resulted in just a 5 percent savings in generation costs, consumers would see more than a \$1.50 decrease in their average monthly bills. If the generation savings from reduced congestion were 10 percent, the average monthly bill for consumers would drop by \$4.00.

So, a small increase in transmission investment can reap a much more significant benefit in lower generation costs.

In addition to investments to relieve congestion, investments in new technology to help improve the control and use of existing transmission lines is critically important.

Revise the Tax Code to Encourage Transmission Investment

While we appreciate that the tax provisions in the energy bills originated in other committees, we want to call your attention to several critical tax provisions that will help increase investment in our transmission infrastructure.

The U.S. tax code should be amended to provide enhanced accelerated depreciation (from 20 to 15 years) for electric transmission assets, similar to the tax treatment governing other major capital assets. Currently, transmission assets receive less favorable tax treatment than other critical infrastructure and technologies. In addition, Congress should ensure that electric companies that sell or otherwise dispose of their transmission assets into a FERC-approved RTO or ITC do not suffer tax penalties. Accelerated depreciation provisions are included in the House version of the pending energy legislation; both the House and Senate versions of the bill address transmission sales or dispositions. We strongly urge inclusion of both of these provisions in the final version of the energy bill.

Conclusion

As I stated earlier, an adequate transmission infrastructure, governed by mandatory reliability rules, is essential regardless of whether wholesale competition or retail competition exists or whether electric companies are vertically integrated or disaggregated. Our challenge is to work together to make sure the transmission system is

robust enough to keep the lights on and provide consumers with affordable, reliable electric service no matter what industry structure model exists. The utility industry is currently investing billions of dollars a year in upgrading our transmission infrastructure. But, clearly more needs to be done. We urge Congress to adopt badly needed reforms to our federal electricity laws to help facilitate reliability and investment in, and construction of, our energy infrastructure.