Framework for the Continuing Development of a Competitive Wholesale Market for the Benefit of Consumers
Edison Electric Institute Board of Directors
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The Current Situation

Regulatory authority over US electricity markets is divided between state and federal authorities and is likely to remain so for the foreseeable future. The United States Congress, through the Energy Policy Act of 1992, endorsed the development of competitive wholesale markets and the Federal Energy Regulatory Commission (FERC), through Order Nos. 888, 889, 2000, 2003 and 2004, created a roadmap for how to provide consumers with just and reasonable rates under wholesale competition. At the federal level, FERC is promoting policies for the development of competitive wholesale electric markets capable of serving large regions.

States are responsible for the regulatory structure for providing retail electric service, but have different views on what is the best model, which largely reflect regional considerations. Currently, about one-third of the states provide for retail competition and two-thirds do not.

States and FERC want to assure just and reasonable rates to their customers and to assure there are adequate electric generation resources. States want to continue to take the lead on policies concerning electric resource adequacy and procurement relating to fuel supply choices and environmental aspects of electric generation.

EEI's Framework

EEI companies support pursuing more effective wholesale markets throughout the United States because properly structured competitive wholesale markets benefit consumers. Robust wholesale competition offers the potential of substantial benefits to consumers in terms of lower costs, greater efficiency in the use of generation and transmission resources, and enhanced reliability.

The benefits of robust wholesale competition can be achieved only if a strong, effective state-federal working relationship is established on all

regulatory matters that provide the stability and certainty needed to attract investment.

Within this context, any framework for wholesale competition should include the following elements:

Effective Wholesale Competition Needs a Robust, Reliable Transmission Infrastructure

- All market participants should be subject to mandatory, enforceable reliability standards that are developed or approved by the North American Electric Reliability Council (NERC), with oversight and enforcement by the Federal Energy Regulatory Commission.

- To attract the capital necessary to build sufficient transmission capacity: (1) FERC's transmission rate polices should be reformed to provide proper incentives and cost allocations; (2) the Public Utility Holding Company Act (PUHCA) should be repealed, with appropriate federal and state access to books and records; and (3) the tax code should provide the appropriate incentives, including accelerated depreciation, to attract capital investment.

- To facilitate the siting of transmission infrastructure: (1) FERC should have backstop siting authority if states cannot or will not act on applications to build transmission to relieve critical transmission bottlenecks and (2) the Department of Energy (DOE) should act as lead agency to coordinate all authorizations and environmental reviews required under federal law to site transmission facilities and to set deadlines for federal reviews.

- To facilitate regional initiatives, like those involving new multi-state transmission, resource adequacy or Regional Transmission Organization (RTO) formation, there should be effective regional coordination. Regional State Committees can play an important role, but should not create another layer of regulation.

There Must be Fair and Open Access to Transmission

- All transmission-owning utilities should be subject to the same level of FERC regulation to assure fair, open access for all market participants to the transmission grid.

- The transmission system should be operated in a fair and non-discriminatory manner.

- Many of the Nation's transmission systems are under the control of an RTO or an Independent System Operator (ISO). States and FERC play a significant role in decisions relating to the formation and expansion of RTOs. Where RTOs are not formed, fair and non-discriminatory transmission access should be achieved by state and FERC endorsed mechanisms, which might include independent transmission administrators, transcos or similar organizations. Market monitors should also provide for oversight over matters such as the behavior of market participants and assurance of independence, transparency and fair open access.

- Regardless of whether transmission is controlled by an RTO, ISO, independent system administrator, or other similar organization, rules and practices should be transparent and the transmission system should be operated efficiently.

- Transmission pricing should (1) allow for cost recovery of fixed and variable costs and a reasonable return on transmission investment; (2) eliminate the pancaking of rates within an RTO region; (3) ensure that cost responsibility follows cost causation; (4) minimize the potential for cost shifting and (5) permit the recovery of all prudently incurred transition costs, and (6) promote efficient siting of new transmission and generation facilities.

Efficient Wholesale Markets Require Fair Rules for Competitive Transactions

- Effective market monitoring, enforcement, and consumer protections should be in place for competitive wholesale markets. Market monitors should be independent of market participants and transmission operations management and should have the authority to report directly to FERC and state regulators.

- Competitive market rules should not favor one corporate structure, business model or retail regulatory model over another. Many different structures and business models can coexist in a competitive wholesale marketplace provided there are fair rules in place for all market participants.

- Under the Federal Power Act, it is FERC's responsibility to prevent the exercise of market power in competitive wholesale markets and to develop the rules for such markets. Any analysis of market power in wholesale markets should take into account existing commitments and obligations under state law and state policies relating to service obligations, resource procurement, resource adequacy, fuel supply choices and environmental aspects of electric generation.

- Affiliates should be allowed to compete in competitive procurements conducted by regulated utilities to serve their own retail customers. Transactions with affiliates should be conducted in a fair and transparent manner to protect against bias and favor to the affiliate of such a regulated utility.

- A reasonable competitive resource procurement process should be in place which explicitly recognizes both FERC's jurisdiction over wholesale transactions and state jurisdiction over retail service, planning, resource adequacy, fuel supply choices, environmental aspects of electric generation and retail cost-recovery issues.

- Regional market structures should provide accurate price signals to promote efficient investment and ensure long-term resource adequacy. Provisions should be made for long-term resource adequacy that reflect the regulatory and market structures adopted by the states within a region. In competitive markets, this may require market mechanisms to ensure long-term resource adequacy.

- Market rules should allow for reasonable credit and risk management policies.

- In traditional regulated retail markets, states should continue to seek innovative policies to encourage efficient, low cost operations.

Under Any Market Structure, the Following Policies are Critical to Achieve Efficient Low-Cost Service to Electric Customers:

- Regulators should provide sufficient certainty in their rules and decisions to stimulate long-term investments by avoiding after-the-fact revisions, decisions that implement a "lower of cost or market" approach or decisions that transfer uncompensated risks to utilities.

- States should fairly address provider of last resort, reliability backup and related cost recovery issues.

- Federal regulators should recognize the retail service obligations of utilities and promote policies consistent with those state imposed obligations.

- State and federal efforts to promote cost-effective conservation and efficiency investments to benefit consumers should be strongly supported.

- Well designed low income energy assistance programs should be strongly supported.

- Federal and state energy and tax policies should promote fuel diversity and further development of renewable energy, energy efficiency improvements, nuclear energy, and clean coal technologies.

- PURPA's mandatory purchase obligation should be reformed because it distorts markets and increases electricity prices to consumers.