The Honorable Spencer Abraham
Secretary of Energy
U. S. Department of Energy
1000 Independence Avenue, SW
Washington, DC 20585

August 7, 2003

Re: Proposal to Establish a Federal Control Area from Within the California ISO Control Area

Dear Mr. Secretary:

We wish to express serious concerns regarding the proposal by the Western Area Power Administration (WAPA) to establish a separate electric power control area from within the current California ISO Control Area. This proposal has been driven, in part, by the impending expiration of contract obligations between WAPA and Pacific Gas & Electric Corp. (PG&E). We believe that adoption of such a proposal is contrary to current federal policy goals for improved integration and coordination among electricity systems, and will instead further balkanize the Western Grid.

The direction of federal energy policy on this subject is unambiguous. One of the stated goals of the Federal Energy Regulatory Commission's (FERC) Wholesale Market Platform concept is to expand the scope of regional markets. The April 2003 FERC White Paper on this subject states that "[r]egional operation is critical for both reliability and efficiency because power flows freely throughout regional grids."[1] The Department of Energy's (DOE's) own report to Congress on Standard Market Design (SMD) indicated that regionalization was a laudable goal.[2] Further, the DOE National Transmission Grid Study also affirms that regional operation and planning of transmission is essential for ensuring reliable and affordable electricity, both now and in the future.[3] Establishment of a separate WAPA Control Area is diametrically opposed to these policy goals. The FERC White Paper, mentioned above, also stresses the importance of avoiding "having customers pay multiple, cumulative charges for transmission service across multiple utility grids in a region. The rate paid by a customer should permit that customer to have access to the entire region at a single rate." However, the establishment of multiple, cumulative charges appears to be precisely what WAPA plans to do.

While FERC and your Department may have limited ability to compel state-regulated or municipally-owned utilities regarding issues of integration and Regional Transmission Organizations, there have been FERC-led efforts to create various incentives for such utilities to further federal electricity policy goals. We can only hope

[1] U.S. Federal Energy Regulatory Commission, *White Paper, Wholesale Power Market Platform*, April 28, 2003.
[2] U.S. Department of Energy, *Report to Congress: Impacts of the Federal Energy Regulatory Commission's Proposal for Standard Market Design*, DOE/S-0138, April 30, 2003.
[3] U.S. Department of Energy, *National Transmission Grid Study*, May 2001.

that the actions of federal power marketing agencies, such as WAPA (over which the Department does have considerable influence), would be consistent with federal electricity policy. Unfortunately, some of the WAPA proposals directly and specifically contradict national energy policy goals in the areas of regional transmission integration, coordination, economic streamlining and the avoidance of duplicative transmission charges (*i.e.*, pancaking). The WAPA control area plan would require the investment of tens of millions of dollars for what appear to be duplicative facilities, the possible condemnation and purchase of portions of two substations, or even the construction of a redundant substation.

Another potential component of WAPA's plans is the recovery of at least some of its increased PG&E transmission charges and facilities costs through a new transmission charge to be imposed on any power flows through WAPA-owned facilities. In particular these new charges would be applied to the major north–south transmission path between California and Oregon. Such plans raise significant concerns about impacts on equity, efficiency, and competition in California. The WAPA-owned components are only a subset of the facilities that now comprise the California Oregon Intertie (COI) that is currently managed as a single interface. The WAPA proposal would effectively result in two different pricing regimes for what is presently treated as a single transmission path. This creates a new set of economic 'seams issues', not only between control areas, but *within* control areas. It is hard to imagine how the efficiency of transmission pricing would not suffer from such a retrograde step. Increased transmission prices that are unrelated to costs restrict trade and thereby potentially harm both the competitiveness and efficiency of the regional market.

The expiration of WAPA's 1967-vintage transmission-service contract with PG&E means that WAPA will face increased costs no matter what proposal is adopted. The equity questions about how these, and other, legitimately incurred increases in costs should be distributed are complicated and we will not directly address them here. We do urge that, however those questions are resolved, any new charges are imposed in ways that do not create new 'seams issues' or artificially inflate the marginal cost of transmitting electricity into/out of or within California.

There are reliability implications to the creation of a new control area in the heart of the California ISO. The ability of the system operators to react to and control system disturbances may be impaired because of the increased communications that are necessary to interact with another control area. We believe that it would be poor public policy to support further fragmentation of the Western U.S. grid, when there appears to be no clear net benefits from such an action.

In summary, we urge the Department to consider not only the narrow question of WAPA's near-term decisions but also the implications of those decisions for Federal policy for the electricity industry. If indeed the DOE determines that the overall public interest is best served by creating a new WAPA control area, what does this imply for the Department's other commitments to policies that encourage other utilities to follow an opposite course?

It is also important to recognize that opposition to WAPA's control area proposal is neither a rejection nor reaffirmation of California's electricity restructuring policies. The ownership and control of Federal generation facilities is not at issue. What is at issue is the proper scope for the control and coordination of regional transmission facilities that serve a collection of utility, non-utility, and Federally-owned producers. Even in areas dominated by regulated utility producers, the benefits of a broader scope for regional transmission coordination have been well understood. For the reasons listed above, we strongly support a policy that maintains WAPA as part of the California ISO control area.

Sincerely,

The Market Surveillance Committee of the California ISO (MSC)

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CC:

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