

**BEFORE THE  
UNITED STATES SENATE**

**COMMITTEE ON ENERGY AND NATURAL RESOURCES**

**TESTIMONY OF THE HONORABLE MARSHA H. SMITH  
COMMISSIONER, IDAHO PUBLIC UTILITIES COMMISSION**

**ON BEHALF OF THE  
NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS**

**ON**

**“State of the Nation’s Electric Transmission Grid”**

**July 31, 2008**



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Good morning Chairman Bingaman, Ranking Member Domenici, and Members of the Committee:

My name is Marsha H. Smith, and I am a member of the Idaho Public Utilities Commission (IPUC). I also serve as President of the National Association of Regulatory Utility Commissioners (NARUC), on whose behalf I am testifying here today. I very much appreciate the opportunity to appear before you this morning and offer a State perspective on transmission issues.

NARUC is a quasi-governmental, non-profit organization founded in 1889. Our membership includes the State public utility commissions serving all States and territories. NARUC's mission is to serve the public interest by improving the quality and effectiveness of public utility regulation. Our members regulate the retail rates and services of electric, gas, water, and telephone utilities. We are obligated under the laws of our respective States to ensure the establishment and maintenance of such utility services as may be required by the public convenience and necessity and to ensure that such services are provided under rates and subject to terms and conditions of service that are just, reasonable, and non-discriminatory.

There are many challenges to resolve prior to the development of the much needed growth in the transmission system that is so vital to reliable electric service, our economic growth, and our national security. Without greater development of and increased capacity in the transmission systems, our efforts to assemble the energy resources that will be necessary, should we embark on a policy that will constrain carbon

emissions, may not achieve the desired results. Additionally, it has been projected that the demand for electric energy in the United States will grow by more than 30 percent over the coming decades. Significant upgrades will be necessary in order to meet this demand. Solutions to the current transmission challenges facing us are not quick, simple, noncontentious, inexpensive, nor, in some cases, obvious. Finding and implementing solutions will require cooperation by, not confrontation among, the various stakeholders. I would now like to address a few specific issues with regard to the state of the nation's transmission grid.

### **Congestion Study and NIETCs**

The Energy Policy Act of 2005 (EPAct 2005) required the Department of Energy (DOE) to conduct a study of electric transmission congestion one year after the legislation was enacted, and every three years thereafter.<sup>1</sup> After considering alternatives and recommendations from interested parties, DOE must issue a report, based on the study, which may designate any geographic area experiencing electric energy transmission capacity constraints or congestion that adversely affects consumers as a national interest electric transmission corridor (NIETC).<sup>2</sup>

The first DOE Congestion Study was issued on August 8, 2006. On April 26, 2007, the DOE issued two draft NIETCs – the Mid-Atlantic Area National Corridor (some or all counties in Delaware, Ohio, Maryland, New Jersey, New York,

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<sup>1</sup> Section 216(a)(1) of the Federal Power Act (FPA).

<sup>2</sup> Section 216(a)(2) of the FPA.

Pennsylvania, Virginia, West Virginia, and the District of Columbia); and the Southwest Area National Corridor (seven counties in southern California, three counties in western Arizona, and one county in southern Nevada). On October 2, 2007, DOE finalized the designations of both NIETCs - the Mid-Atlantic Area National Interest Electric Transmission Corridor (Docket No. 2007-OE-01) and the Southwest Area National Interest Electric Transmission Corridor (Docket No. 2007-OE-02). DOE affirmed the NIETC designation orders on March 10, 2008.

### *NARUC Perspective*

At a July 18, 2006 Annual Pacific North West Economic Region Summit in Edmonton, Alberta, Canada, DOE listed the following principles during an “Ending the Stalemate” presentation:<sup>3</sup>

1. The initial round of NIETC designations should focus on the most congested areas in the country;
2. The NIETC designations must have clear and supportable boundaries;
3. The NIETC designations must be defensible and demonstrate due diligence – by both the DOE and regional planning entities;
4. DOE should not issue an NIETC designation until it has the information needed to bound an NIETC appropriate to the underlying problem;

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<sup>3</sup>See “Ending the Stalemate” July 18, 2006 DOE presentation at <http://pnwer.dataweb.com/tables/jointables/meetingparticipantjoin/files/presentation/souder.pdf#search=%22DOE%20Alberta%20corridors%22>.

5. Congress did not intend for DOE to become a planning or siting agency. The NIETC designations should not be route-specific, and siting should be left to those who have siting authority;
6. The NIETC designations should support, not conflict with, efforts and conclusions by regional planning entities; and
7. The NIETC concept is intended to overcome obstacles to transmission expansion, not impose new ones. The NIETC process must therefore be timely and simple.

NARUC's comments to DOE expressed its concern that the Congestion Study does not adequately conform to these principles or the express terms of the agency's statutory charge. In order to remedy these deficits, the agency should, at a minimum, (1) perform a more granular analysis of congestion prior to designating a specific NIETC and (2) work cooperatively with the various regional planning organizations and the affected States within each region. Specifically, a review of the Congestion Study highlighted the following problems:

1. The Congestion Study Methodology, without further review and explanation, should not provide the basis for any NIETC Designation;
2. EPCRA 2005 Section 1221 requires a full and productive consultation with affected States before DOE makes any NIETC designations;
3. There should be deference to areas with mature regional planning processes;

4. DOE should consider solutions other than transmission, such as initiatives to expand demand-response programs and relieve congestion problems and transmission constraints before making an NIETC designation; and
5. An NIETC designation should not be made unless cost allocation concerns have already been resolved.

NARUC appreciated the DOE Secretary's decision to solicit comments before taking final action on any specific NIETC designations. We commended the Secretary's attention to the comments made by NARUC members and State regional organizations on the Draft NIETC designations. NARUC did not make specific comments to DOE on either Draft NIETC; rather, NARUC focused on two general issues:

1. The default 12-year term for a NIETC Designation should be modified to a default three-year term to conform with the issuance of the Congestion Study; and
2. Clarification on DOE's authority under Federal Power Act (FPA) Section 216(a)(2) to designate a conditional area of congestion based solely on projections of future congestion.

NARUC did not appeal either the DOE Congestion Study or the NIETC designations. There are, however, pending appeals by individual States, regional, and national environmental groups of both NIETC designations in a number of federal district and appellate courts.

## *Western Perspective*

The Western perspective is that the designation of the Southwest NIETC was based on anecdotal information and information from various transmission studies, not a systematic review of historical flow data provided by the Western Electricity Coordinating Council (WECC), the regional reliability organization.<sup>4</sup> The breadth of the Southwest NIETCs, especially in southern California and western Arizona is too sweeping. DOE failed to develop objective metrics that would determine when there is congestion that would warrant a NIETC designation. The various measures WECC provided to DOE did not show any consistent pattern that would indicate one path in the West is more congested than any other. The Western Interstate Energy Board's Committee on Regional Electric Power Cooperation (CREPC) invited DOE to hold a workshop to develop metrics to define congestion. To date, it has not been held. Such a selective use of information undermines acceptance of a DOE designation.

In any case, the primary concern over adequate transmission in the West is not existing congestion; rather, it is future congestion that will result from locating new power plants. DOE has told its staff not to consider future congestion as part of their

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<sup>4</sup> See CREPC comments at [http://www.westgov.org/wieb/reports/crepc/07-06-07CREPC\\_comments\\_SWNIETC.pdf](http://www.westgov.org/wieb/reports/crepc/07-06-07CREPC_comments_SWNIETC.pdf) and WECC comments at [http://www.westgov.org/wieb/reports/crepc/07-06-07TEPPC\\_comments\\_SWNIETC.pdf](http://www.westgov.org/wieb/reports/crepc/07-06-07TEPPC_comments_SWNIETC.pdf). The Western Governors Association (WGA) passed a Resolution that says: "The Western Interstate Energy Board is to report to the Governors on whether the Department of Energy's designation or proposed designations of NIETCs in the West is based on sound analysis and information and whether such designations adequately incorporate information from state and regional renewable energy zone studies... The WGA staff and the Western Interstate Energy Board are directed to develop potential recommendations to the federal government on policy changes needed to enable the region to move renewable energy generation to market, including but not limited to changes to Sections 368 and 1221 of the Energy Policy Act of 2005, and changes to FERC Order 890." The full Resolution is at <http://www.westgov.org/wga/policy/08/electricity8-8.pdf>.

2009 Congestion Study required by EAct 2005. Currently, DOE is in the process of preparing for the 2009 study and is holding regional workshops to consult with States and other stakeholders. During the first Western workshop in San Francisco on June 11, 2008, many participants raised similar points about congestion metrics and the need to be forward looking about analyzing congestion. The WECC transmission planning group, Transmission Expansion Planning Policy Committee (TEPPC) plans to take a closer look at congestion metrics in preparation for the 2009 Congestion Study.

DOE should be putting more emphasis on the implementation of EAct 2005 Section 1221(h). Federal agencies are the major cause of delay in transmission permitting in the West. This was true before the passage of the legislation, and remains the case. Aside from an interagency MOU, the federal agencies have not done much more to fix the problem. As to EAct 2005 Section 368, the idea of designating NIETCs across federal lands is a good one. Unfortunately, the federal agency work thus far is likely to be out-of-date and irrelevant when the NIETCs are finalized. Much has changed regarding fuel choices since the passage of the legislation. For example, the focus in the West is on renewable generation, not new coal plants. But, the proposed NIETCs were largely based on existing right-of-ways or transmission plans that had coal plants as the anchors of any new transmission. DOE should redo the Section 368 corridor work once the Western Governors Association's Western Renewable Energy Zones (WREZ) work is completed and load-serving entities (LSEs) indicate which zones they are interested in.

The geographic location of my home State makes it important to the future development of transmission in the western grid. Idaho has entered into a “Cooperating Agency Status” with the lead federal agency, the Bureau of Land Management, on the Gateway West Project. Obviously, access to federal lands is critical to the success of this venture. At 1.6 to 2.6 million dollars per mile, decisions that reroute transmission paths can result in extraordinary costs to consumers. The reality is that customers ultimately pay for transmission projects. Transmission is the key to insuring energy security and new generation resources (renewable, nuclear, natural gas, *etc.*) are dependent upon new transmission development.

### **Siting**

A major impediment to siting energy infrastructure, in general, and electric transmission, in particular, is the great difficulty in getting public acceptance for needed facilities. This tells us that no matter where siting responsibility falls – with State government, the Federal government, or both – as prescribed in the EAct 2005, siting energy infrastructure will not be easy and there will be no “quick fix” to this situation.

During the EAct 2005 debate, NARUC opposed the “backstop siting” provision. NARUC’s position prior to passage of EAct 2005 was, and continues to be, that to have the greatest economical and environmental benefits transmission facilities should not be nationalized; practical considerations require they be regionalized and that this regionalization should be encouraged, not required. Just as States have a role in the siting

of interstate highways, States need to continue having an active role in transmission decisions.

EPAct 2005 gave federal backstop siting authority of certain electric transmission facilities to the Federal Energy Regulatory Commission (FERC).<sup>5</sup> Upon NIETC designation by DOE, FERC may issue permits to construct or modify electric transmission facilities if FERC finds that:

- (1) A State in which such facilities are located does not have the authority to approve the siting of the facilities or to consider the interstate benefits expected to be achieved by the construction or modification of the facilities;
- (2) The applicant is a transmitting utility but does not qualify to apply for siting approval in the State because the applicant does not serve end-use customers in the State; and
- (3) The State with siting authority takes longer than one year after the application is filed to act, or the State imposes conditions on a proposal such that it will not significantly reduce transmission congestion or it is not economically feasible.

To issue a permit, FERC must find that proposed facilities:

- (1) are used for interstate commerce;
- (2) are consistent with public interest;

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<sup>5</sup> Section 216 of the FPA.

- (3) significantly reduce transmission congestion in interstate commerce;
- (4) are consistent with national energy policy; and
- (5) maximize the use of existing towers and structures.

As Congress considered of EAct 2005, NARUC expressed deep concern with the language that eventually became Section 1221. At that time, NARUC opined that the language would in essence overrule legitimate State agency concerns and laws with regard to how a State ruled on a transmission project. The language would then permit FERC to vacate the decision and preempt State law and actions. Whether our initial observations and fears were accurate will only be determined by future decisions of FERC. FERC issued the Final Order – Order No. 689 – implementing its backstop siting authority on November 16, 2006.

### *NARUC Perspective*

In its comments on the FERC rulemaking, NARUC said it expects that the backstop siting authority will have limited applicability because the majority of the State commissions have the authority to approve or deny, as the case may be, proposed transmission projects within their jurisdictions and because State commissions are frequently allowed to address the interstate benefits of proposed projects. Furthermore, many State statutes require a petitioner to obtain a certificate of public convenience and necessity, or some other similar certificate, from a State commission before constructing

transmission facilities regardless of whether the applicant provides electric service to end-use customers. NARUC proposed that:

1. FERC clarify that federal backstop siting authority under FPA Section 216 is only triggered when the State Commission fails to or cannot act in a timely manner;
2. FERC clarify how it will apply the federal backstop criteria;
3. The proposed rule be revised to implement the due process requirements of the statute; and
4. The Final Rule adopted should incorporate a reference and deference to extensive siting records developed at the State level to prevent duplication and confusion.

The Final Order gives the States one full year to consider a transmission line siting application before the federal pre-filing process begins. The intent is to avoid conducting “parallel proceedings” – where a State commission and FERC would be considering a siting application at the same time. If such “parallel proceedings” were allowed, that process would create *ex parte* and prejudgment concerns under State law. Such a situation could potentially result in an applicant “gaming” the siting process by purposefully filing a deficient application to the State with the hopes of starting the one-year federal clock and precluding adequate State consideration of the application. NARUC did not appeal the FERC backstop siting rule. There are pending court appeals by individual States of this rule.

### *Western Perspective*

The Western perspective is that Congress needs to clarify that if a State turns down a transmission line proposal for good reason and within a reasonable timeframe, FERC should not be able to second guess the State. In Order No. 689, FERC voted 4-1 in favor of saying that Congress did not care if a State acted timely or reasonably. FERC Commissioner Suedeen Kelly dissented by saying it was incomprehensible that Congress intended FERC to override timely State decision. Additionally, it only seems fair that the one-year clock for State action needs to be suspended whenever a federal agency is the cause for the State delay in a permitting decision.

### **Cost Allocation**

State regulators are concerned about transmission reliability, adequacy, and the costs required to support the development of robust competitive wholesale markets. The investment that is needed to upgrade the nation's transmission grid in order to support expanded wholesale power markets will cost billions of dollars. Notwithstanding the general benefit to the wholesale electric marketplace of encouraging the construction of new generating capacity and its interconnection to the grid, it is also important to provide proper price signals to encourage optimal demand response and promote economic and efficient expansion of the transmission grid and siting of generation. The FERC has in the past adopted transmission pricing policies that generally provide for the direct assignment of costs to the parties causing the costs.

FERC Order No. 2000 stated the "[m]arket designs that base prices on the average or socialization of costs may distort consumption, production and investment discussions and ultimately lead to economically inefficient outcomes."<sup>6</sup> FERC has departed, in some instances, from a transmission pricing policy that provides for the assignment of costs to the cost-causative parties. In general, NARUC supports efficient pricing policies that result in the economic use and expansion of the transmission systems to support a robust wholesale electricity market. We recognize that transmission investments needed to maintain the reliability of the existing transmission systems should continue to be recovered through transmission rates charged to all transmission users. We advocate that the cost of upgrades and expansions necessary to support incremental new loads or demands on the transmission system should be borne by those causing the upgrade or expansion to be undertaken, except that FERC should not preclude the assignment of interconnection cost to the general body of ratepayers within a State when that State's regulatory body determines that such allocation is in the public interest.

A robust regional electric transmission system is an essential prerequisite to support a) reliability and b) the market function allowing more generators to reach loads and compete directly for wholesale sales to such loads in order to increase competition among generation suppliers and meet national goals for renewable generation and energy independence. A new rate design is needed that will facilitate the construction of the strong transmission backbone required to support the nation's wholesale electric markets, future increases in renewable generation capacity, and reliability.

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<sup>6</sup> Order No. 2000 at pp. 642-3.

## **Incentive Rates**

Pursuant to Section 1241 of EPAct 2005, which adds a new FPA Section 219, FERC proposed a rulemaking to amend its regulations to establish incentive-based rate treatments for the transmission of interstate electric energy by public utilities to ensure reliability and reduce the cost of delivered power by reducing transmission congestion. NARUC's comments to FERC discussed the factors, other than the absence of incentive-based rate treatments that affect the level of transmission system investment, offered a framework for implementation of the new FPA Section 219, and discussed the role of research and development in encouraging the use of new technologies.

In particular, NARUC said that the Final Rule should require certain showings as a prerequisite for an award of incentives and provide that the amount of incentives awarded in connection with any particular project will not exceed the amount necessary to obtain construction of the proposed facilities. By specifying the purposes for which incentives are available and requiring FERC-jurisdictional rates to remain just and reasonable,<sup>7</sup> Congress has clearly recognized the risks to customers involved in incentive rate awards. We said that FERC should carefully limit the availability of incentives to projects of the type specified in FPA Section 219 to reduce the risk that consumers will be forced to pay higher rates for the construction of facilities that would have been built regardless of the availability of an incentive or that do not provide substantial benefits to customers. FPA Section 219(a) clearly establishes that authorized "incentive-based rate

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<sup>7</sup> FPA Section 219(d) provides that "[a]ll rates approved under the rules adopted pursuant to this section, including any revisions to the rules, are subject to the requirements of Sections 205 and 206 that all rates, charges, terms, and conditions be just and reasonable and not unduly discriminatory or preferential."

treatments” are intended to facilitate the construction of new transmission facilities that either ensure reliability or reduce the cost of power by reducing congestion. NARUC asked FERC to include language in any rule adopted in this proceeding to ensure that a successful applicant for incentive-based ratemaking treatments must prove to the Commission that the proposed transmission facilities would not be constructed in the absence of an incentive award and that the proposed facilities will either materially improve reliability or materially reduce the overall cost of power by reducing transmission congestion. A failure to make the necessary showing will result in a denial of the application for an incentive award. Congress’s recognition of these limitations on the availability of incentives is appropriate given that some transmission investment will occur with or without incentive support and because the construction of new transmission facilities may not invariably improve reliability or reduce costs to a degree appropriately reflective of the cost of the project.

Furthermore, while certain of the incentives proposed inherently specify the amount of the incentive to be awarded, the same is not true of other proposed incentives. As a result, NARUC asked that FERC should specify in its Final Order that the amount of incentives awarded in connection with any particular project will not exceed the amount necessary to obtain construction of the proposed facilities. FERC issued the Final Order – Order No. 679 – on July 20, 2006.

For an example of the implementation of the FERC transmission incentives rule, please see the New England Conference of Public Utility Commissioners (NECPUC)

involvement in the Docket: Docket No. ER08-69-000. One of the concerns recently voiced by the NECPUC was that applying rate of return adders to the actual cost of a project, regardless of how much the project's eventual cost exceeded original estimates, would create perverse incentives by rewarding transmission owners for bringing projects in *over* budget. On June 12, 2008, NECPUC filed a complaint with FERC in that Docket pointing out that the costs of many of the projects that FERC had ruled eligible for rate of return adders are now double and triple their originally estimated levels. The resulting cost of the incentive adder to ratepayers, NECPUC observed, would be far greater than FERC could have anticipated when it approved the adder. NECPUC urged FERC to prevent this result by limiting the adder to the transmission owner's original estimated cost. Because rapidly rising costs of material and construction is a nationwide phenomenon, FERC's ultimate disposition of NECPUC's complaint may have significant ramifications beyond New England. While we expect the Commission to fully consider the merits of these critical issues as it addresses the NECPUC complaint, this case may illustrate the extent that the policies Congress adopted in 2005 should be reexamined in light of changing market conditions.

In conclusion, there is much to be done to ensure that this nation avoids an "electric transmission crisis." The solutions to the challenges will not come quickly or easily. Finding these solutions will require cooperation by, not confrontation among, the various stakeholders, including State and federal government . Thank you and I look forward to your questions.