

Commission on Electric Utility Restructuring  
June 29, 2004, Richmond

The first meeting of 2004 of the Commission on Electric Utility Restructuring focused on the status of regional transmission entities, also known as regional transmission organizations (RTOs).

RTOs are entities created to operate transmission grids and ensure short-term system reliability, independent of control by incumbent utilities and other market participants. RTO independence is intended to ensure that incumbent utilities, which traditionally controlled the generation, distribution and transmission of electricity, do not use the control of transmission assets to favor their generation arms over competing suppliers. As such, they are viewed as necessary to the development of a competitive retail market for electric generation. Virginia's Electric Utility Restructuring Act, as amended in the 2003 Session, requires incumbent utilities to transfer ownership or control of their electric transmission assets to an RTO between July 1, 2004, and January 1, 2005, subject to the approval of the State Corporation Commission (SCC).

PJM's Perspective

Philip F. Abraham, representing PJM Interconnection, LLC, a Pennsylvania-based RTO, updated the Restructuring Commission on the status of the efforts of Dominion Resources and AEP to join PJM. AEP filed its application with the SCC on December 19, 2002, and Dominion filed its application on June 27, 2003. Hearings on AEP's and Dominion's SCC applications are scheduled to start on July 27, 2004, and October 12, 2004, respectively.

AEP's efforts to join PJM prompted the Federal Energy Regulatory Commission (FERC) to initiate a proceeding on November 25, 2003, in which FERC asserted that § 205(a) of the Public Utilities Regulatory Policy Act (PURPA) authorized the federal agency to exempt AEP from requirements of the Restructuring Act, including those requiring that the SCC approve any transfer of a utility's ownership or control of transmission capacity to an RTE. PURPA § 205(a) provides that the FERC is not authorized to exempt utilities from a state law that is designed to protect the public health, safety or welfare, or the environment, to conserve energy, or to mitigate the effects of fuel shortages.

On June 17, 2004, the FERC issued its opinion affirming its initial decision that it has the authority to permit AEP to integrate into PJM notwithstanding Virginia's laws, rules and regulations, and setting October 1, 2004, as the date for AEP to join PJM. The FERC noted that it will not exercise its authority to integrate AEP into PJM if the SCC timely finds that AEP completes its proceedings in time to meet that deadline and reaches agreement regarding reasonable conditions that do not prevent or prohibit integration.

Jim Hinton of PJM testified regarding the benefits that would accrue from AEP and Dominion joining PJM. These include improving management of the electricity transmission grid through mandatory reliability rules and centralized dispatch of generation and control of power systems. PJM membership would also enhance reliability of the electricity transmission grid, attract new power supply and transmission investments, reduce wholesale energy prices, and implement

demand response programs. Mr. Hinton praised PJM's congestion management pricing system as ensuring that costs are borne by entities causing the costs rather than by all consumers. He claimed that investments in new generating resources are occurring in PJM's proposed footprint, which extends from Northern Illinois to North Carolina's Outer Banks, as evidenced by the 4,000 MW of capacity currently under construction.

Mr. Hinton noted that participation in PJM's wholesale markets is voluntary, and that participants have realized advantages where its markets have been deployed. In response to questions regarding PJM's perspective on the protection of native load, he observed that member utilities have exercised self-supply and bilateral contract options to comply with states' concerns that native loads be protected from the possibility that low-cost power could be sold for greater profit in high-cost markets.

### AEP's Perspective

Craig Baker of AEP noted that AEP's commitment to join an RTO was a condition for approval of its merger with another utility, and reiterated that RTOs are seen as a necessary ingredient of effective retail consumer choice programs. Though AEP's system-wide costs of joining PJM will be between \$50-55 million annually, the company's studies show that these costs are slightly exceeded by the financial benefits. AEP chose PJM as its RTO because of its sophisticated markets that will facilitate retail competition, PJM's impressive reliability record, and the benefits of having a single RTO manage the transmission systems of AEP and Allegheny Power in the congested West Virginia-Virginia border area. PJM's system was described as compatible with AEP's power pool, and AEP will be able to continue to provide power for its own retail customers on a cost basis, rather than a market price basis, while it will be able to sell its surplus power in the market.

With respect to the pending hearing on AEP's request for SCC approval of its application to join PJM, Mr. Baker stated that the parties have reached an impasse in attempting to negotiate a settlement. AEP did reach a settlement with Kentucky regulators, which addressed concerns regarding assurances that PJM's markets are and would remain voluntary, that in the event of a power shortage AEP's power supplies would not be shifted to other states to the detriment of its customers, that reliable transmission was available to serve native loads, and that Kentucky was not ceding any of its jurisdiction.

### Dominion's Perspective

Thomas Farrell of Dominion noted that his firm is involved in three separate proceedings relating to RTO membership before the SCC, the North Carolina Utilities Commission, and the FERC. The company's goal is to turn over control and management of its transmission system to PJM by November 1. In May 2004 PJM and Dominion filed an application with FERC to form the PJM South RTO, which provides in part that transfer of control of transmission assets is conditioned upon FERC's approval of a request that it be authorized to sell energy and capacity at market-based rates within its service territory. In addition, Dominion has sought to condition the transfer of control of transmission assets to PJM upon FERC's approval of a request that Dominion be permitted to defer for future recovery of approximately \$240 million in costs

associated with RTO membership. Dominion is seeking to defer expensing these costs until the end of the capped rate period under the Restructuring Act, January 1, 2011. In response to a question by Senator Watkins, Dominion stated that in its FERC case it is asking only for permission regarding the deferred accounting treatment for these expenses, and acknowledged that their recovery would be determined in a rate proceeding at the end of the capped rate period.

Mr. Farrell and Christine Schwab, Dominion's Director of PJM Integration, stated that PJM will result in value added for Dominion's customers. The benefits include greater reliability and enhanced retail and wholesale competition. Greater access to surplus power from other areas within PJM will result in a reduced need to build generation facilities as well as the ability to procure imported power at lower prices than Dominion could charge. An analysis by Charles River Associates concludes that Dominion's membership in PJM will result in a reduction in Dominion's revenues of between \$281-537 million and net savings to Virginia retail customers of between \$255-464 million over the period from 2004 to 2014.

In response to questions regarding the ability to withdraw from PJM, Dominion's representatives cited the decision of the D.C. Circuit Court involving Atlantic City, in which FERC was held not to have the authority to bar a member from withdrawing. In such event, a member may withdraw by simply filing a new transmission tariff with the FERC.

The Restructuring Commission's next meeting, scheduled for September 8, will be conducted jointly with the Virginia Coal and Energy Commission.

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