UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Financial Reporting and Cost Recovery Practices for Regional Transmission Organizations and Independent System Operators	)	Docket No. RM04-12-000

COMMENTS OF THE EDISON ELECTRIC INSTITUTE
AND THE ALLIANCE OF ENERGY SUPPLIERS

The Edison Electric Institute and its affiliated Alliance of Energy Suppliers (collectively EEI) respectfully submit these comments in response to the "Notice of Inquiry" (NOI) issued by Federal Energy Regulatory Commission (FERC or the Commission) on September 16, 2004.[1]

EEI is the association of the nation's shareholder-owned electric utilities, international affiliates, and industry associates worldwide. Our U.S. members serve more than 90 percent of the ultimate customers in the shareholder-owned segment of the industry, and nearly 70 percent of all electric utility ultimate customers in the nation. They generate almost 70 percent of the electricity generated by U.S. electric utilities.

Many EEI members are transmission providers subject to the jurisdiction of the Commission, including a substantial number who are also members of Independent

[1] *Financial Reporting and Cost Accounting, Oversight and Recovery Practices for Regional Transmission Organizations and Independent System Operators,* Notice of Inquiry, 108 FERC ¶ 61,237, 69 Fed. Reg. 58112 (2004).

System Operators (ISOs) or Regional Transmission Organizations (RTOs). In addition, many EEI members either directly, through affiliate power producers, or both, own electric generation facilities that provide electricity to wholesale markets subject to Commission regulation. The Alliance of Energy Suppliers represents investor-owned electric energy suppliers and marketers nationwide, including affiliate and independent power producers who also own generation facilities that provide electricity to wholesale markets regulated by the Commission. The Alliance is a division of EEI that specifically represents unbundled, bundled, and independent power suppliers. EEI members, thus, include both transmission providers and transmission customers who would be affected by any changes the Commission might adopt to adjust the current practices of ISO, RTO, and member utility accounting, financial reporting, and cost recovery practices.

EXECUTIVE SUMMARY

In EEI's view, the Commission is correct to explore whether there are ways to improve the transparency and accountability of RTOs/ISOs. As a relatively new component of the nation's electricity delivery system and marketplace, RTOs/ISOs are still evolving. Each is different from the other in significant ways, and those differences partly reflect variations in the nature of the markets and transmission grids in different regions of the country as well as in policy choices by states and market participants in those regions. Yet RTOs/ISOs undertake many similar functions and incur similar types of costs, and unnecessary differences can create inefficiencies. So some degree of uniformity in recordkeeping and reporting is appropriate.

At the same time, the Commission needs to avoid unnecessarily imposing new information collection and reporting burdens on the RTOs/ISOs, and their members. Those burdens themselves come at a substantial cost. RTOs/ISOs and their members already keep extremely detailed financial records under the Commission's Uniform System of Accounts (USofA) and report large volumes of that information to the Commission in the FERC Form 1 and other periodic reports. Any call for more information must be well founded and well justified.

Likewise, the Commission should not impose new regulatory requirements on the governance, operation, or efficiency of RTOs/ISOs. Under the D.C. Circuit's recent California ISO decision,[2] there are limits on how far the Commission can go to specify governance practices. Nor should the Commission want to get involved in the operation of RTOs/ISOs in that level of detail.

Instead, to improve RTO/ISO recordkeeping, reporting, cost management, and cost recovery, EEI recommends that the Commission make the following improvements:

(1) Provide direction to RTOs/ISOs as to the proper USofA accounts or subaccounts where they should record typical categories of income, expenses, assets, and liabilities, relying on existing accounts and subaccounts to the maximum extent possible;

(2) Compile a list of "best management practices" used by different RTOs/ISOs aimed at ensuring open, accountable budgeting and financial management;

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[2] CAISO v. FERC, 372 F.3d 395 (2004).

(3) Encourage each RTO/ISO to work closely with market participants during the development of its annual budget and to provide them with an annual report focusing on the coming year's budget, supplemented by quarterly summaries comparing budgeted versus actual expenditures, allowing comments by the market participants; and

(4) Encourage use of periodic voluntary surveys completed by RTO/ISO members to gauge RTO/ISO performance and to identify areas for improvement.

Such measures would assist RTOs/ISOs, utility participants, and policymakers in comparing RTOs/ISOs and ensuring that they provide necessary services at reasonable cost. But these measures would be relatively unobtrusive.

As part of the annual and quarterly reporting process, the Commission should provide guidance on the form of the annual and quarterly reports in order to facilitate benchmarking. Further, the Commission could provide a statement that the RTO/ISO costs thus reviewed are reasonable and prudent transmission/wholesale costs entitled to be recovered in RTO/ISO member utility rates. In addition, the Commission should urge the National Association of Regulatory Utility Commissioners (NARUC) to support the use of rate adjustment mechanisms to ensure timely recovery of transmission costs in retail rates. Such a determination of reasonableness and support for cost recovery would be very helpful. At least one MISO transmission owner has had Midwest ISO Schedule 10 costs disallowed due to an alleged absence of proof.[3]

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[3] Minnesota Public Utility Commission Docket E001/GR-03-767, Interstate Power and Light.

To develop these proposals in more detail, EEI recommends that the Commission convene a technical conference and work closely with RTO/ISOs and market participants on these issues. EEI and our members would be more than willing to participate in such a conference and to work with the Commission on these issues. The goal would be to help identify appropriate ways to provide more transparency and accountability to the RTOs/ISOs, in particular their budgeting and financial management processes, without impeding their formation and evolution.

BACKGROUND

In its NOI, the Commission is exploring the need for changes to its accounting and financial reporting requirements for RTOs/ISOs and the utilities that belong to them. The Commission also is exploring the need for further Commission oversight, benchmarking, or other measures to ensure that RTOs/ISOs have incentives to be cost efficient and that their costs remain reasonable from a ratepayer perspective.

RTOs/ISOs are charged with overseeing the operation of transmission grids and wholesale markets in their geographic areas of the country. To varying extents they also participate in a resource planning function to help ensure the continued adequacy of the grid, though market participants make ultimate generation and transmission facility decisions with regulatory oversight by state utility commissions and FERC, among others.

Despite ordering open access transmission service for the electric industry with the issuance of Order No. 888, and encouraging the formation of RTOs with the issuance of Order No. 2000, the Commission has never promulgated specific accounting rules or rate review principles for RTOs/ISOs. Instead, the Commission has relied upon its existing rules and policies, which were developed to apply to traditional public utilities principally consisting of investor-owned utilities. Thus, though the USofA was developed for traditional public utilities, because RTOs/ISOs are public utilities, the Commission has required them to follow the USofA too.[4]

The accounting rules contained in the USofA provide for capturing financial information along the primary functional business lines associated with traditional utility structure. But in its NOI, the Commission has stated that functions typically performed by RTOs/ISOs appear quite different than the functional business segments or service lines of traditional utilities, and therefore use of the Commission's existing USofA to capture and classify costs may result in RTO/ISO financial statements and reports providing insufficient information about costs and their relationship to services provided or other business activities.

In the NOI, the Commission has also noted that differences between RTOs/ISOs have made comparison between them difficult and their not-for-profit status complicates review of their costs.[5] Thus, as the NOI acknowledges, the development of RTOs/ISOs raises fundamental questions about the adequacy of the Commission's current accounting and financial reporting rules and its current rate review practices for RTOs/ISOs. The Commission has initiated this proceeding in order to explore whether changes to the RTO/ISO accounting, financial reporting, and cost recovery principles are necessary to

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[4] *See PJM Interconnection, L.L.C.*, 107 FERC ¶ 61,078 (2004).

[5] The Commission noted that it has previously observed that the "Midwest ISO's non-profit status complicates prudence review after the costs are incurred." *See Midwest Independent System Operator*, 101 FERC ¶ 61,221 at P 35, *order on reh'g*, 103 FERC ¶ 61,035 (2003).

ensure that rates charged by RTOs/ISOs and their member transmission-owning public utilities are just and reasonable.

COMMENTS

I. Accounting and Financial Reporting Issues for RTOs/ISOs

A. General Remarks

EEI supports standardization of RTO/ISO accounting and financial reporting to the Commission, in line with accounting definitions currently used by utilities and other market participants, and is willing to work with the Commission's staff to address the specific improvements that should be made in applying the USofA to RTOs/ISOs. Standardization of application of the USofA by RTOs/ISOs will provide greater transparency and comparability of RTO/ISO budgeting practices and expenditures. EEI also proposes that RTOs/ISOs should post on their websites financial statements that compare "actual" and "budget" details.

EEI does not support significant changes to the USofA. Instead, rather than making substantial changes in the USofA or imposing new layers of regulation on RTOs/ISOs and their members, EEI recommends that the Commission focus its attention on providing guidance to RTOs/ISOs relating to their use of the existing USofA that will result in greater standardization in the accounting and reporting by the RTOs/ISOs. This might be accomplished by providing a list of the key types of income, expenses, assets, and liabilities RTOs/ISOs typically have, along with direction as to the proper USofA accounts or subaccounts where these financial items should be logged. At most, the Commission may need to identify a select number of new sub-accounts for the

RTOs/ISOs to use in order to reflect their typical more significant financial income, expenses, assets, and liabilities.

B. EEI Responses to Commission Questions

Question 1. Are the individual account descriptions and instructions under the existing USofA adequate for the functions typically performed by RTOs/ISOs? If not, what changes should be made to the account descriptions and instructions under the existing USofA to accommodate the RTO/ISO business model? Are the changes so extensive that an entirely separate USofA should be developed to accommodate RTOs/ISOs?

Answer 1. EEI supports clarifying the existing USofA – both account descriptions and instructions – to allow for consistent, standardized reporting by the RTOs/ISOs. The Commission could provide this guidance to RTOs/ISOs though a framework of the key types of income, expenses, assets and liabilities that RTOs/ISOs typically have, along with direction as to the proper USofA accounts and subaccounts that should be used for financial transactions.

Question 2. Under the existing USofA costs are accounted for as electric production, transmission, distribution or general plant. What other accounts and functional classifications should be provided for RTO/ISO transactions and events? For example, are additional revenue, expense or detailed fixed asset accounts needed?

Answer 2. EEI supports clarifying the current USofA to provide for better and more consistent reporting of RTO/ISO transactions and events. The possible use of subaccounts by RTOs/ISOs could be reviewed to complement the existing accounting and reporting. This would be a good topic for discussion at the technical conference we are encouraging the Commission to convene.

Question 3. Should the Commission develop a new financial reporting format for the functions typically performed by RTOs/ISOs? If so what financial information and financial-related information should be reported? If not, how may the existing annual and quarterly financial reports be changed or modified to report relevant RTO/ISO transactions and events?

Answer 3. EEI supports standardization of reporting by RTOs/ISOs to the Commission to increase the transparency of their financial condition through the existing annual Form 1 and quarterly Form 3-Q. The Commission could designate certain accounts and subaccounts that would only be used by RTOs/ISOs in their reporting. Standardization will also enhance the budgeting process for RTOs/ISOs. Again, this would be a good topic for discussion at the technical conference.

Question 4. Is additional accounting and financial reporting guidance needed for market operation and market monitoring functions of RTOs/ISOs? If so what transactions and events require additional accounting and financial reporting guidance?

Answer 4. EEI suggests that this topic can be covered at a technical conference.

Question 5. Is there sufficient detailed financial and financial-related information being provided to users of RTO/ISO data? If not, what additional information would the users of the information find helpful and why? For example, if detailed information technology cost data is necessary, would it also be helpful for the RTO/ISO to include the cost driver of the data (*e.g.*, quantity of desktop computers in relationship to the number of employees)?

Answer 5. As covered later in the comments, EEI believes that the RTOs/ISOs should have a transparent budget process and frequent disclosures of cost information, including projections and actual information. In addition, the RTOs/ISOs should disclose data necessary to calculate performance measures on a consistent basis, to facilitate benchmarking and efficiency analyses. EEI also proposes that RTOs/ISOs should post on their websites summary annual and quarterly financial statements that compare "actual" and "budget" details with commentary on significant differences.

Question 6. Currently the quarterly and annual Commission financial reports include a schedule that requires respondents to report data concerning the transmission of electricity for others. Should RTOs/ISOs report transmission of electricity for others for its Commission-jurisdictional members or should those individual members report the information in their individual filings? If the RTO/ISO should report the information, what information should be reported and how should it be shown in the filing?

Answer 6. EEI supports the reporting of transmission of electricity for others by RTOs/ISOs in the annual Form 1 and the quarterly Form 3-Q. The most efficient solution would be for RTOs/ISOs to provide this information directly to the Commission instead of providing it to all of the transmission owners who then provide the information to the Commission. It would also be most efficient for the RTOs/ISOs to report the monthly peak load information in the annual Form 1 and the quarterly

Form 3-Q. The same point also applies to other Commission reports, such as the FERC Electric Quarterly Reports (EQRs) required of Commission-jurisdictional RTO/ISO members. A large quantity of data required for the FERC EQRs relates to sales that are made through RTOs/ISOs. But in general , the RTO/ISO sales data are not kept in a format that is easily compatible with the EQR template. As a result, reporting companies must download tens of thousands of lines of RTO/ISO data and re-work the data into the EQR format. It would be far better for the RTOs/ISOs to submit their information in their own EQRs directly, thus relieving RTO/ISO members of having to undertake the additional work while also reducing the likelihood of error or omission.

II. Accounting and Reporting Issues for Public Utility and Licensee RTO/ISO Participants

A. General Remarks

In our view at this time, changes are not needed to the USofA for public utilities and licensees because the USofA is well-developed to fully reflect the utilities' and licensees' revenues and expenses.

B. EEI Responses to Commission Questions

Question 1. Are the individual account descriptions and instructions under the existing USofA useful and applicable for classifying revenues received from RTOs/ISOs? If not, what changes should be made to the account descriptions and instructions under the existing USofA to accommodate these transactions and events?

Answer 1. EEI believes that the existing USofA account descriptions and instructions are adequate for the recording of revenues from an RTO/ISO.

Question 2. Are the individual account descriptions and instructions under the existing USofA useful and applicable for classifying costs related to providing various services such as ancillary services, energy markets, or costs associated with transmission congestion? If not, what changes should be made to the existing USofA to accommodate these transactions and events?

Answer 2. EEI believes that the existing USofA account descriptions and instructions are adequate for recording costs from an RTO/ISO.

Question 3. What additional detailed information should be collected or disclosed in the quarterly and annual Commission financial reports of individual utilities to provide greater transparency of RTO transactions and events?

Answer 3. EEI does not believe that additional information needs to be provided in the annual Form 1 or quarterly Form 3-Q.

Question 4. What additional disclosures should be made in the quarterly and annual Commission financial reports of individual utilities to describe the economic effects resulting from the respondent transmitting public utility participating in an RTO?

Answer 4. EEI does not believe that additional disclosures should be required in the annual Form 1 or quarterly Form 3-Q. If the Commission wants an economic study on RTO/ISO participation, such a study should <u>not</u> be part of the accounting and financial reports of an RTO/ISO.

Question 5. Does the Commission's USofA and existing financial reporting requirements for public utility members of RTO/ISOs provide regulators with adequate information to clearly identify which functions are performed by the RTO/ISO and which are performed by the member transmission-owning public utilities, and to ensure that costs are not being double recovered through either Commission-jurisdictional or state-jurisdictional rates? Are they adequate to determine how RTO/ISO costs billed to public utility members should enter into the determination of retail rates? If not, what changes to the Commission's accounting and reporting rules should be made?

Answer 5. EEI believes that the existing USofA account descriptions and instructions are adequate for the recording of costs from an RTO/ISO. EEI suggests that there should be no presumption that because an RTO/ISO is accumulating costs in an account or subaccount, a utility cannot have costs in the same account or subaccount. If warranted, this topic could be discussed further in the technical conference. In addition, recovery of RTO/ISO charges in retail rates can be problematic. For example, if a state has implemented a rate freeze, any increase in transmission-related revenue requirements may not be recoverable in retail rates; at least, not until the freeze expires. Even without an explicit freeze, states may seek to offset transmission revenue increases with decreases in other legitimate revenues. To ensure timely recovery, states and the Commission need to work together to coordinate revenue requirements and rate designs. One good solution would be to implement an adjustment mechanism that separates transmission revenues from other retail revenues, and ensures that transmission costs are recovered timely in retail rates. We urge the Commission to encourage NARUC to support rate adjustment mechanisms to ensure timely recovery of transmission costs in retail rates.

III. RTO/ISO Cost Management Issues

A. RTOs/ISOs Present Unique Cost Management Issues

RTOs/ISOs do not face a number of the cost constraints that market participants face. In particular, RTOs/ISOs are largely funded by market participants,[6] so they are buffered from market forces they otherwise would face in seeking to finance their operations and to recover their costs with a reasonable rate of return. In addition, as transmission and wholesale market entities, they are not directly regulated by states, so they do not face retail rate pressures that other market participants face.

As a result, it is very important for the Commission to continue to promote RTO/ISO budgeting and financial management processes that are open, transparent, and accountable to the market participants who pay the RTO/ISO bills. The Commission already requires each RTO/ISO to have an independent board of directors and to consult with an advisory committee made up of all classes of market participants prior to taking action. The Commission has also stated that it expects RTO/ISO boards "to be proactive" on cost control and "to guard against any unreasonable costs being incurred."[7] But beyond that, the Commission's focus on ISO/RTO expenditures has been primarily reviewing cost allocation and rate design methodologies.[8]

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[6] The Commission noted in the NOI that one exception is that PJM earns money for its members when it sells software and technology to other transmission providers. However, as with other RTOs/ISOs, PJM otherwise passes through its costs of operation to its market participants.

[7] See Midwest Independent System Operator, Inc., 101 FERC ¶ 61,221 at P 3 (2002).

[8] The Commission has required MISO to file its annual budget and make progress reports on expenditures related to market development for informational purposes. *See Midwest Independent System Operator*, 101 FERC ¶ 61,222 (2002), *order on reh'g*, 103 FERC ¶ 61,035 (2003). The Commission explained that these informational filings would "provide a sufficient opportunity to review and compare the proposed costs with the actual costs and allow the Commission to monitor the Midwest ISOs cost containment efforts." *Id.* at P 36.

The Commission should consider taking further steps, as described in the next sections of these comments. As the Commission has noted in its NOI, at least some RTO/ISO stakeholders have raised concerns that the advisory committee process provides an insufficient check because stakeholders may see the budget only after it is finalized and they have no veto power. Even the advisory committees have no ability to veto an action of the RTOs/ISOs but are limited to offering non-binding advice on budget and other matters. Furthermore, because RTOs/ISOs currently recover their costs from market participants via Commission-approved tariffs and rate schedules, the Commission's normal refund remedy for addressing costs "after the fact" does not work well in the RTO/ISO context – all costs incurred by the RTOs/ISOs have to be passed on. In fact, imposing such a remedy could actually harm the market participants, potentially making it more difficult for them to recover the costs in retail rates.

B. EEI Encourages the Commission to Consider Three Improvements in RTO/ISO Budgeting and Financial Management

To address these concerns, EEI encourages the Commission to take three additional steps. In addition to requiring an independent board and stakeholder advisory committee, the Commission should: (1) compile a list of "best management practices" used by the various RTOs/ISOs to promote open, accountable budgeting and financial management; (2) promote use of cost-review processes that allow effective periodic stakeholder review of and meaningful input regarding RTO/ISO expenses, and (3) encourage use of voluntary surveys completed by RTO/ISO members to gauge RTO/ISO performance and identify areas for improvement.

First, as described in the next section of these comments, we recommend that the Commission compile a list of "best management practices" used by the various RTOs/ISOs for ensuring that their budgeting process and financial management are as open and accountable as possible. The Commission should provide this list as guidance to each RTO/ISO and encourage RTOs/ISOs to adopt similar practices.

Second, as part of this initiative, the Commission should identify key elements of a streamlined cost review process for RTOs/ISOs. Each RTO/ISO should be encouraged to provide stakeholders an annual cost assignment form that supports projected RTO/ISO costs for the coming 12 months. The form should provide detailed projected costs, including the costs of labor, consultants, hardware, software, benefits, and facilities. Interested parties should have the opportunity to provide input to the development of each annual form, as well as have an opportunity to comment on the end result. Such a forward-looking process would give stakeholders the opportunity to address budget concerns before the fact. In addition, the Commission should encourage or require RTOs/ISOs to develop five-year long-range plans as the backdrop for the annual budget process and filings.

Third, the Commission should encourage an independent third party identified by stakeholders within each RTO/ISO to conduct periodic surveys of RTO/ISO market participants, to be completed voluntarily by the market participants, as a way to compare the effectiveness of RTO/ISO operations and areas for improvement. An RTO/ISO's failure to complete basic functions such as settling and clearing markets, dispatching load, and issuing bills in an accurate and timely manner can increase costs, impede market transactions, and discourage investment in new facilities. The surveys could enable market participants to assess the relative effectiveness of their own RTO/ISO and ways to improve its operations.

C. FERC Should Provide "Best Management Practice" Guidance on Open, Accountable RTO/ISO Budgeting and Financial Management

In order to ensure that RTO/ISO administrative and transmission operation services are cost-effective, RTOs/ISOs should develop their budgets and manage their finances in an open, accountable stakeholder process, supported by proper cost accounting as previously discussed. Taken together, an open, accountable budget/financial management process and proper accounting should enable an appropriate balance between RTO/ISO efficiency and RTO/ISO independence.

To help ensure that the RTO/ISO budget/financial management processes are open, transparent, rational, and accountable, the Commission should compile a list of best management practices used by the various RTOs/ISOs and proposed by stakeholders to achieve these goals. Further, the Commission should provide this list to the RTOs/ISOs as guidance on ways to improve their individual budget/financial management processes.

The goal is to have RTOs/ISOs provide meaningful checks on their budgeting and spending decisions – in advance through the budget and financial management process. A well-designed and implemented "before the fact" budget/financial management process, which provides market participants with adequate information and the ability to provide meaningful input, is the only effective way of controlling costs. An "after the fact" process simply will not work, given that RTO/ISO costs are borne by the market participants. Any costs that the Commission might find ex post facto to be imprudent would still be costs the RTO/ISO has incurred and would have to be paid by the market participants. Moreover, an ex post finding of imprudence could affect the ability of a market participant, such as a utility distribution company that is charged such costs, to recover them at retail. While the Commission should maintain its role to respond to specific stakeholder challenges to RTO/ISO expenditures, such challenges should be rare if the Commission encourages an open, transparent, and rational budgeting/financial management process in the first place.

To achieve an open budget/financial management process, it is critical that RTOs/ISOs provide stakeholders with specific, timely information so the stakeholders can participate effectively in the process. Current RTO/ISO processes have not always provided stakeholders with adequate or timely information. This has left some parties without adequate recourse to address potential grievances related to RTO/ISO incurred costs.

At the same time, the Commission should not pre-approve RTO/ISO budgets or micromanage their programs. Instead, the Commission should encourage transparency and accountability in the RTO/ISO budget/financial management process by providing policy guidance on ways to improve the process. The Commission should begin by canvassing RTOs/ISOs and stakeholders to identify "best management practices," focusing on such topics as:

(1) Ways to design and implement RTO/ISO budgeting/financial management processes to ensure that stakeholders can participate effectively in the processes.

(2) Types of information that may be useful to stakeholders, including annual budgets, quarterly and annual financial statements, quarterly summaries comparing budgeted versus actual expenses, advance notice of material deviations from the budget, and long-range plans so stakeholders can develop an appropriate understanding of the budget.

(3) Categories of information stakeholders need, focusing on the typical revenues and expenses discussed in section I of these comments, recognizing that RTOs/ISOs must accumulate cost control data with sufficient detail and present the data in a form that can be used for practical analysis by stakeholders.

(4) Techniques for providing information to stakeholders early and timely enough so they can participate effectively in the budget/financial management process, including for example through use of electronic distribution or websites.

(5) Use of RTO/ISO cost/operating activity-based accounting and performance measures, based on consistently defined information, to assist RTOs/ISOs and others in benchmarking RTOs/ISOs.

(6) Recommendations as to financial expertise of RTO/ISO staff who participate in the budgeting/financial management, including the need for a chief financial officer who is well qualified and free of potential conflicts with market participants.

(7) Techniques for ensuring that stakeholders are able to provide input on major new initiatives through a process that allows costs and benefits of the activity to be fully examined, including for example use of registered voting by the stakeholders.

In time, if the Commission remains concerned about whether RTO/ISO budget/financial management processes are sufficiently open, transparent, rational, and accountable, the Commission may wish to revisit this issue. If the best management practice and other guidance suggested in these comments do not suffice, the Commission may need to consider adopting additional measures, such as a more stringent budget and expense approval process, perhaps even requiring RTOs/ISOs to make filings with the Commission before making large expenditures. However, such measures are not warranted at this early stage.

D. EEI Responses to Commission Questions

Question 1. Do not-for-profit RTOs/ISOs currently have the appropriate incentives to contain costs? If not, what are the right incentives (and why would they be the right incentives) and how should they be implemented?

Answer 1. While RTOs/ISOs are not subject to the financial accountability imposed by for-profit market discipline and state retail rate regulation, at the same time not-for-profit RTOs/ISOs do not have an incentive to spend more than needed to carry out their duties. More rigorous focus on budget preparation and disclosure of actual to budget comparisons will serve to heighten the importance of operating cost containment without sacrificing the ability of the RTOs/ISOs independently to administer the competitive markets for the benefit of all stakeholders.

Question 2. Should the Commission revisit the means by which RTO/ISO rates are reviewed, particularly with respect to cost incurrence? If so, what means should the Commission employ to ensure that RTOs'/ISOs' expenditures are prudent and their rates are just and reasonable? Would a "best practices" or "benchmark" approach, where one RTO/ISO's expenditures in a particular cost category are measured against those of other RTOs/ISOs, be sufficient?

Answer 2. As noted above, the most effective approach to controlling RTO/ISO costs will be greater consistency in accounting and a more transparent budget process. Furthermore, requiring on-going RTO/ISO dissemination of budget and cost information to stakeholders, including comparisons of budgets to actual expenditures, will also facilitate transparency. Such filings should contain sufficient detail to allow stakeholders and the Commission to make meaningful and informed judgments about the reasonableness of proposed and actual expenditures. If the Commission later finds that RTOs/ISOs lack an open, transparent and rational budget/financial management process, the Commission could consider additional measures, even perhaps requiring the RTOs/ISOs to file their budgets with the Commission and giving stakeholders an opportunity to comment. Before considering any benchmarking of RTO/ISO expenditures, the Commission should first simply provide guidance to RTOs/ISOs on classifying and accounting for costs, recognizing the differences between RTOs/ISOs.

Question 3. What is the appropriate role for the Commission with respect to overseeing RTO/ISO software costs? Should an RTO/ISO be required to justify contracting for the development of new software rather than using or modifying "off-the-shelf" software developed for a comparable application for or by another RTO/ISO? To what extent would the use of standardized or at least compatible software in neighboring RTO/ISO markets reduce the cost of doing business across RTO/ISO boundaries? How would any such standardization be accomplished?

Answer 3. The Commission should not single out RTO/ISO software costs for special oversight, but should encourage RTOs/ISOs to use existing software wherever possible in lieu of developing redundant programs or programs that are unnecessarily inconsistent from RTO to RTO. At the same time, RTOs/ISOs should be open to adopting and sharing with each other innovative improvements in software. Nevertheless, if stakeholders have raised significant concerns relating to the costs associated with software incurred by any specific RTO/ISO, the Commission should be prepared to increase its oversight role with regard to that specific RTO/ISO.

Question 4. To what degree should an RTO/ISO's stakeholder/advisory committee be involved in reviewing or shaping the RTO/ISO's budget and spending decisions? Are there independence considerations that should prevent or limit such review by market participants?

Answer 4. As discussed in sections III.B and III.C of these comments, stakeholders should be involved in the RTO/ISO budgeting and spending process to the greatest extent permissible while preserving the Commission-required independence of the RTO/ISO from market participants. In cases where stakeholders raise significant concerns relating to their level of involvement with a specific RTO/ISO, the Commission should continue to provide a forum to address these issues, for example through the complaint process.

Question 5. Should the Commission allow differences between RTOs/ISOs with regard to cost allocation and rate design to recover the operation and capital costs for each of their functions (e.g., tariff administration and markets for energy, ancillary service, and FTRs)? If so, how should the various rates be designed, i.e., what are the correct billing determinants for each service?

Answer 5. Yes, in order to accommodate regional variations, the Commission should allow differences between RTOs/ISOs with regard to cost allocation and rate design. The Commission should continue to allow individual RTOs to determine how various rates are to be designed for their regions, subject to Commission review. However, such regional variations should not create unnecessary seams.

Question 6. Should the compensation of senior RTO/ISO management be linked to specific performance measures, including cost reductions?

Answer 6. As a general matter, at least a portion of RTO/ISO management compensation should be tied to performance based on measurable goals and objectives, which would include cost controls. The Commission should encourage RTOs/ISOs to use performance-based incentives. However, the Commission should not become involved in the process of determining appropriate compensation or performance measures. The RTO/ISO board should be responsible for establishing appropriate compensation and performance measures.

TECHNICAL CONFERENCE

The proposed accounting guidelines, best management practices, cost reporting requirements, and effectiveness surveys to which we have alluded above can be developed through a technical conference. The conference should involve input from each RTO/ISO, their participating utilities, and other market participants, ideally including individuals with accounting and management expertise.

The technical conference could develop consensus definitions for common RTO/ISO income, expenses, assets, and liabilities; and directions in terms of which USofA accounts and subaccounts to use to record specific kinds of transactions. Any new sub-accounts needed to record common RTO/ISO transactions could be identified as part of the conference deliberations. Most importantly, the conference could address uniform reporting formats to facilitate benchmarking of RTO/ISO cost performance.

Similarly, the technical conference could focus on recommendations for budgeting and financial management processes that provide adequate participant access and input to the development of budgets and to the management of costs (e.g., related to major software development projects), while preserving RTO/ISO operational independence in terms of providing non-discriminatory access to transmission.

CONCLUSION

EEI appreciates the chance to submit these comments, and we encourage the Commission to incorporate them fully into any order the Commission may issue in this proceeding. If the Commission has any questions about the comments, please contact me or any of the following EEI staff involved in their preparation: Henri Bartholomot (202/ 508-5622), Tim McClive (202/ 508-5085), David Stringfellow (202/ 508-5494), Aryeh Fishman (202/ 508-5023), Eric Ackerman (202/ 508-5528), or Tonja Wicks (202/ 508-5098).

Respectfully submitted,

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