

## TESTIMONY



**TESTIMONY OF  
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PRESIDENT AND CEO,  
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L.L.C.  
HEARING ON THE IMPACT OF  
ELECTRIC INDUSTRY  
RESTRUCTURING ON SYSTEM  
RELIABILITY  
UNITED STATES SENATE  
COMMITTEE ON  
GOVERNMENTAL AFFAIRS  
JUNE 28, 2001**

Mr. Chairman, members of the Committee. We are in a critical time in the evolution of the electric industry. In reaction to the California crisis, we can travel down the path of revised regulation of electricity and create vast new command and control structures to ensure the delivery of this vital product to the American consumer. Or we can roll up our sleeves and use the lessons of past missteps and the lessons of success to reaffirm a commitment to finding the best market-based solutions that deliver value to customers. We need solutions that can withstand the test of use, both in good times and bad.

My name is Phillip Harris. I am the President and CEO of PJM Interconnection. We operate the largest centrally dispatched electricity market in the country and the third largest in the world. We manage the reliability of the high voltage electric power grid and

operate the world's most successful market for electricity. We serve approximately 8.7% of the U.S. population in a five — soon to be seven — State region stretching from Washington D.C. to the northern border of New Jersey and into Ohio.

We were recently designated by *Business Week* as one of the top 50 businesses in the United States successfully integrating Internet technologies into our business — the only utility to receive such designation. In the PJM region, the restructuring experience has worked. Customers have saved money and enjoy more choices and improved service. Investors are flocking to our region and have announced more than 140 new generating projects, which would add over 40,000 MW of generation to our region, as well as over \$700 million in new and upgraded transmission investment. The attached article from *The Wall Street Journal* outlines in greater detail some of the measures of the PJM success story. Moreover, I would like to reserve the right to supplement this testimony with additional material concerning analyses of the PJM story for the hearing record.

The key to PJM's success has been following our "four-R's". Implementing:

**Real Markets operating in**

**Real Time supported by**

**Real information producing**

**Real Results.**

**Let me focus on each of those.**

**Real Markets Operating in Real Time---**

**Electricity is not like any other product. It is the only product that is instantaneously produced and consumed and travels at the speed of light. The North America electric system is comprised of three interconnections — as illustrated in the attached map — that are, in effect, three synchronous motors operating at the speed of light. Thus any solution needs to take into account the physics of the electric grid.**

**In addition we have a legacy of local practices from the large number of separate electric companies, each of which operated as their own control area. Finally, we have a history of local, State and Federal regulation of this industry. Our challenge is to combine the physics, the local practices, and the legal requirements to devise solutions for reliability “AND” competitive markets.**

**At PJM, we have devised such “AND” solutions. In the reliability arena we have done so by not artificially dividing up what is reliability versus what are the needs of the market. Rather, on a minute-by-minute basis, 7 days a week, 24 hours a day, our operators balance and harmonize the needs of reliability and the market.**

**Accordingly, we have the following specific recommendations on how this Committee can work with the FERC to ensure “AND” solutions:**

- a. We believe that the FERC should have authority over all of the different market participants when it**

comes to reliability, including the Federal power marketing agencies, municipals, co-operatives, and investor-owned utilities.

b. FERC needs to oversee both sides of the equation. If we pigeonhole what is reliability and assign that to one institution and markets to a second institution, we just create a new set of barriers to customer value;

c. FERC needs to vigorously enforce its Order 2000. If we compromise on the basic structures needed to make markets work, we will have to make costly patches after the fact, as we see in California. This is not the time to “dumb down Order 2000”;

d. Make sure that the RTOs have planning authority and undertake it in an independent and open manner. Transmission and generation compete with one another. If there is not trust that the planning process is being carried out in a neutral and independent way, we will fail to build the vital infrastructure needed to make the market function well;

e. FERC’s focus needs to be on developing markets. We have spent a lot of time addressing structural issues. Although they can be important, form follows function. We need to focus on the key ingredients to making the market work;

f. Ensure that FERC is fully staffed and has the resources to appropriately monitor the markets and regulate in those areas where the market is not properly functioning .

g. The nation is moving rapidly to networked information through advanced technology. FERC should have these and the staff resources to use them in order to identify and be responsive to market dysfunctions in a timely manner. The FERC staff has begun this effort, but more will be needed as markets develop.

**Addressing those recommendations, we**

believe that as part of the “AND” solution it is critical that FERC challenge and hold the newly-created RTOs accountable for balancing reliability and the marketplace. If we create one set of institutions that focus on reliability, while others focus on markets, we run the risk of having our left hand and right hand not working in harmony. Each will be going its separate way, sending confusing signals to the marketplace and to the consumer, and we have just created new seams issues. I believe this is one of the lessons of California, where the power exchange was separate from the ISO. We should not make that same mistake again, but instead recognize that reliability and the needs of the marketplace are intertwined. We need for the two to work together and be subject to comprehensive FERC oversight.

Real Information---At PJM we have proven that if we get critical information out to the marketplace in a timely manner, we can come up with market solutions that protect consumers. We view ourselves as an information company. We post our energy prices and system conditions on our web site and update them every five minutes. Our approach to management of transmission congestion also includes market-based solutions. We have used that information to create markets in the variety of ancillary services that are critical to maintaining reliability.

Moreover, on a longer-term, we are responsible for regional planning. Under the old paradigm, each utility undertook planning on a company-by-company basis and then proceeded with those projects that were deemed to be in its economic interest. There was no requirement for public review or any requirement for an independent planning

**process. FERC Order 2000, properly enforced, provides that the RTO shall have the authority to engage in regional planning. In PJM we work closely with our State PUCs, as well as our market participants, and just issued a regional plan that provided for the previously mentioned new and upgraded transmission investment. It is critical that FERC ensure that the RTOs it approves:**

**a. are truly independent; and**

**b. have the authority and expertise to undertake regional planning in a fair and unbiased manner.**

**Even with these tools in place, I want to be clear that we do not just throw the reliability of this system and consumers to the vagaries of the marketplace. We have an extremely active market monitoring unit that analyzes transactions over our system to detect any market abuses. And our Board has not hesitated to file at the FERC for changes to our market rules to nip any such market abuses in the bud. We are grateful to FERC for promptly acting on our requests and feel that we have established an excellent working relationship that provides for quick response by the regulator and by our independent Board to maintain the integrity and fairness of the marketplace, as well as the reliability of the system. But for this to happen, we need to ensure that FERC has the resources to get the job done. It needs to have the tools in place to monitor the markets for this vital commodity. FERC has begun this process through their real-time computer systems and we intend to work closely with them to ensure that they have the key data and resources to get the job done.**

**Real Results---**At the end of the day, the true test is one of use. Billions of dollars in trades have occurred on our system. Although we have a \$1,000 bid cap in place, 99% of the time our prices have cleared below \$100/MWh, and 71% of the time our prices were less than \$30/MWh. System reliability has improved since we became an independent system operator. In 2000, our region experienced extremely high temperatures in May, usually a month when plants are out for maintenance. Even with these shortages in generation our prices only reached \$400/MWh for 4 hours. And the marketplace is supporting our market, as witness the dramatic number of planned generation and transmission projects in our area.

Our message is simple: with the right tools and with institutions such as the FERC with authority to balance the needs of reliability and the marketplace, we can achieve “AND” solutions that promote the interests of all Americans in seeing reasonably priced, reliable electric service for years to come. Providing FERC with the authority to oversee all market participants to ensure reliability, as well as ensuring that our regulatory model comprehensively focuses on the integration of reliability and the marketplace, will enable us to achieve these real results.

Thank you very much. I look forward to your questions.

[Wall Street Journal Article](#)

[Unites States Energy Map](#)

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