



SOUTHERN CALIFORNIA  
**EDISON**

An EDISON INTERNATIONAL™ Company

**Stephen E. Frank**  
President and  
Chief Operating Officer

May 9, 1997

The Honorable John D. Dingell  
U.S. House of Representatives  
Washington, DC 20515

Dear Mr. Dingell:

Thank you for providing Southern California Edison with the opportunity to share with you our views on the electric utility restructuring issues raised in your letter dated April 10, 1997.

Enclosed are Edison's responses to the eight questions you asked along with a copy of a statement I presented before the Senate Committee on Energy and Natural Resources on March 6, 1997, and a copy of a letter from Edison to Commissioner Neepser of the California Public Utilities Commission.

If I can provide you with any further information, please do not hesitate to contact me at 818/302-2208.

Sincerely,

Enclosures

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**Responses of Southern California Edison Company  
to Questions Submitted by the Honorable John D. Dingell**

Q1. From your company's point of view, is it necessary for Congress to enact legislation bearing on retail competition, and why? If you favor legislation, please outline which issues should be addressed and how you think they should be resolved.

A1. Southern California Edison believes that Congress should enact legislation which mandates States to allow all retail customers to choose their electric generation supplier by a date certain. Such legislation should be based on three fundamental principles: *equity, opportunity, and respect for past commitments*:

- Equity means that all customers must benefit from competition, not just a select few;
- Opportunity means that all parties, including utilities and affiliates, should be able to compete fairly in the new electric marketplace; and
- Respect for past commitments means that utilities should be given the opportunity to recover the investments made and the commitments entered into for the purpose of meeting their obligation to serve customers.

Edison also believes that Congress should provide the States with reasonable guidelines that are not prescriptive and which give States broad latitude in developing their own retail access programs. In doing so, Congress must respect and preserve State actions which implement customer choice as long as such actions are consistent with opening retail markets by a date certain and adhering to the three principles described above.

There are a number of reasons why Congress needs to enact federal legislation. First, a federal mandate is necessary to ensure that all American consumers will obtain the benefits of a competitive electricity market. Without a federal mandate, consumers in some states will be denied the benefits of competition for an indefinite period of time. Second, there are things that only the federal government can do to ensure that all firms have the opportunity to compete on the basis of efficiency and innovation. This means that federal legislation is necessary to address the following issues:

- Repeal the Public Utility Holding Company Act (PUHCA) by a date certain. This is a pro-competitive step that only Congress can take. A few important elements in PUHCA, such as the regulation of affiliate relationships and the issuance of securities, should continue, but under the regulatory responsibility of the Federal Energy Regulatory Commission;
- Repeal prospectively the mandatory purchase requirement of Section 210 of the Public Utility Regulatory Policies Act (PURPA). With the introduction of competition in the wholesale and retail generation services market, this mandate is no longer necessary;
- Ensure reciprocity of opportunity so that competition occurs on a fair basis. It is fundamentally unfair for utilities, or their affiliates, to market power in “open” states, while their “home” states remain “closed” and not subject to competitive forces;
- Clarify that States have the authority to order retail access. Further, federal legislation should confirm that every sale of electricity has a retail component which is subject to state regulation. States should be free to determine the best way to impose non-bypassable charges for the purpose of recovering stranded costs and the costs associated with public purpose programs (e.g. low income, energy efficiency, and renewable energy programs);
- Modify provisions of the federal tax code to ensure a “level playing field.” These changes include, but are not limited to:
  1. Eliminating the ability of public power entities to issue new tax exempt debt for the purpose of expanding outside their traditional service territories; and
  2. Eliminating the “two-county rule” which allows utilities with only two adjacent counties in their service territory to issue tax-exempt debt. This is specially relevant to Edison since there are three Western utilities that enjoy these benefits (San Diego Gas & Electric, Tucson, and Nevada Power);
- Ensure that State implementation of retail competition provides for the transparency of market information and allows all customers, regardless of size, to benefit from the competitive market. To meet these objectives, the California legislature endorsed the creation of an Independent System Operator and Power Exchange. These institutions will ensure that market information, including electricity prices, is available to all that want it, and that customers who choose not to participate in direct access benefit from competition as well. Congress should encourage other States to similarly consider mechanisms which will ensure that their electricity markets are transparent and allow all customers to benefit from retail competition.

The states have an important role in creating competitive generation services markets as well. Congress should allow States to develop their own retail access programs as long as these programs are consistent with the principles of equity, opportunity, and respect for past commitments. Congress must recognize that not all States are alike in terms of generation resources, environmental quality challenges, industrial base, and mix of private and public power. Consequently, states should be allowed to decide local matters such as the phasing-in of customer choice and the unbundling of distribution services. The federal government should focus on doing only what only it can do to ensure the creation of a truly competitive generation services market.

Attachment 1 sets forth a copy of the Statement of Steve Frank, President and Chief Operating Officer of the Southern California Edison Company, which was presented before the Senate Committee on Energy and Natural Resources on March 6, 1997. This statement explains in greater detail the roles we believe Congress and the States should play in developing a competitive generation market.

Q2. If the state(s) you serve has adopted or is considering adopting retail competition, what are your biggest concerns? Please be specific. Indicate how you are dealing with them and any recommendations you may have.

A2. There are no federal impediments that exist today which could prevent the full and complete implementation of California's electricity restructuring law. However, as described above, Congress can take actions to enhance and improve the competitive market which will begin in California on January 1, 1998. We are also concerned that any legislation adopted by Congress should be based on three fundamental principles: *equity, opportunity, and respect for past commitments*.

Q3. Whether or not you favor federal legislation, please indicate your position on the following specific issues (to the extent not addressed in your prior responses):

a. *A Federal mandate requiring states to adopt retail competition by a date certain.* If retail competition is under consideration in the state(s) you serve, do you believe Congress should provide additional direction or authority?

A3a. California has adopted a retail access program which provides for a smooth and fair transition to a new competitive marketplace for electric power beginning

January 1, 1998. However, it is possible that not all States will adopt legislation that allows retail customers to choose their generation supplier. Accordingly, Edison believes that a federal mandate is necessary to ensure that all American consumers will obtain the benefits of a competitive electricity market by a date certain, that all parties, including utilities and affiliates, can compete in the new electric marketplace, and that past utility commitments will be honored. A federal mandate is also necessary to ensure that future electricity markets are fair and symmetrical. Beginning January 1, 1998, electricity sellers from non-choice states will be able to market electricity to Edison's customers in California, but Edison will be denied reciprocal access to their customers. Mandating a near date certain will end this unfair and asymmetrical situation in a short time. We also believe that federal legislation should include reciprocity provisions binding on public and private utilities and their affiliates to encourage States to open up their markets as soon as possible.

b. *Recovery of stranded investment.* If the state(s) you serve already has adopted retail competition, how was this issue addressed and are you satisfied with the outcome? If your state(s) is considering adopting retail competition, how would you recommend that this issue be treated? Do you think Congress should enact legislation relating to stranded cost issues, and if so what would you recommend? Is securitization a useful mechanism for dealing with stranded costs, and whom does it benefit?

A3b. California's electric restructuring plan includes a non-bypassable Competition Transition Charge (CTC), which provides utilities with a reasonable opportunity to recover costs made uneconomic by the change in public utility law and the move to a competitive market. The law provides for a fixed time period (1998-2001) during which electric utilities would have the opportunity to recover - on an accelerated basis - the potentially uneconomic portion of utility-owned generation investments which California utilities made as part of their obligation to serve all customers under state law. Employee-related transition costs, power purchase obligations and certain nuclear-related and other costs would be recovered over a longer time period. Edison believes that the California resolution of the stranded cost issue is fair and equitable. In fact, the California legislature adopted AB 1890 unanimously. This was the result of a consensus-building process comprised of a number of stakeholders including customers, power producers, utilities, and public power.

Congress should address the issue of stranded costs because providing for the recovery of these costs will encourage the most rapid transition to a competitive,

restructured industry, will produce efficient competition, and is the fair thing to do. As FERC Chair Elizabeth A. Moler testified before the Senate Energy and Natural Resources Committee on March 20, 1997, “Federal leadership on the question of stranded cost recovery is essential for a fair and orderly transition to retail competition.” Accordingly, any federal legislation that requires utilities to grant open access to all its transmission and distribution facilities should include a corresponding requirement on state regulators to give the utility a reasonable opportunity to fully recover all legitimate and verifiable wholesale and retail stranded costs, over a time period and in a manner which does not adversely affect the utility’s financial integrity.

Edison believes that any mechanism for dealing with stranded costs must meet three tests: First, the mechanism should enable all generators to compete on the basis of efficiency; second, the recovery mechanism must be constructed so that no customer can escape or bypass their responsibility to pay for their share of the costs associated with the transition; and third, the mechanism must be designed to provide the utility with a reasonable opportunity to recover those costs previously incurred to provide service to its customers.

We believe that securitization can also help facilitate the recovery of stranded costs and the transition to a competitive marketplace. Through securitization, utilities will be able to replace more expensive equity and debt with lower cost AAA-rated asset backed securities. This results in a reduction in the utilities’ cost of capital which will then be passed through to customers in the form of lower rates. Stranded costs continue to be recovered from customers over time in the form of principal repayment on the asset backed securities. However, the cost of capital of the stranded assets will be far less than the cost of capital on other utility assets, providing benefits to customers. In California, utilities will still be at risk for ultimate recovery of all stranded assets due to factors such as time limits on cost recovery, fuel costs, and general inflation.

c. *Reciprocity.* Can states condition access to their retail markets on the adoption of retail competition by other states? Should Congress enact such a requirement? Could such a requirement create an incentive for states with low electric rates not to adopt retail competition, in order to keep cheap power at home?

A3c. It could be argued that, under state law, a state can condition access to its retail markets on the adoption of retail competition by other states. However,

Edison believes that to ensure that a state can condition reciprocal access to its retail markets, federal legislation is necessary.

Federal legislation could authorize the states to impose a reciprocity provision; or, could simply forbid any supplier of electricity from providing electricity to retail customers in a state other than the one in which the supplier is located unless: (1) all transmission and local distribution facilities owned, controlled, or operated by such supplier and its affiliates are themselves operated to provide open and not unduly discriminatory access; and (2) any person generating the electricity to be supplied, and any affiliates of that generator, provide open access to any transmission or local distribution facilities they own, control or operate.

Given that it may be difficult to fully enforce reciprocity provisions, Edison believes that Congress should enact both reciprocity provisions and an early date certain to ensure that competition in the future is fair and symmetrical.

Q4. If Congress enacts comprehensive restructuring legislation, should it mandate “unbundling” of local distribution company services? What effects would this have, and would they differ for various customer classes? Would this entail substantial expense, and who would incur any such costs?

A4. Edison does not believe that Congress should mandate the unbundling of local distribution services. Instead, states should be allowed to determine the outcome of this local issue. The distribution services usually proposed to be “unbundled” are the metering and billing functions. Both these functions are not affected with interstate commerce, but are strictly local services. Accordingly, the federal government should have no role in mandating that these services be open to competition. States are best equipped to make such a determination.

The question of whether and how to unbundle local distribution services largely turns on the role of the regulated electric utility in the future. In California, we believe that the role of the regulated utility must be fully consistent with customer choice, and be comprised of the following:

1. The utility would operate the wires and distribution system in an even-handed, reliable, and regulated way. As a result, the utility enables customers to confidently choose the source from which they want to buy electric energy, whether from the spot market (e.g. the Power Exchange in California) or from any other supplier;

2. The utility would provide regulated energy tariffs under which any customer can purchase electrical energy at the transparent spot (Power Exchange) price without any mark-up. The utility thereby provides important options for those who may not want to engage in direct contractual power purchase transactions with energy suppliers or marketers and who prefer to rely on the utility to perform power purchase functions for them, under regulatory supervision; and
3. To protect its own essential commercial interests, the utility *will need to meter and bill for its products and services*; but in doing so, the utility would give other market participants access to these metering and billing systems at fair, non-discriminatory and regulated prices.

A more detailed description of Edison's view of the future role of the electric utility in California is set forth in Attachment 2. This attachment contains a letter from Edison Vice President Bruce Foster to Commissioner Josiah L. Neeper of the California Public Utilities Commission.

As shown, Edison believes that the regulated utility should retain the right to meter and bill for the products and services it provides. Utilities should not be mandated to give up this right in favor of having metering and billing provided by third parties in the name of competition. Edison is not opposed to other energy suppliers or marketers metering and billing their own customers for the products and services it provides. This is a commercial right that every market participant should be free to exercise. In this same spirit, Edison should not be forced to give up its commercial rights in this area as well.

Edison is also concerned that if distribution unbundling is mandated, that it be done correctly. Prior to unbundling distribution services, the following should be assured:

1. Implement enforceable consumer protection measures, including, but not limited to: a. regulations for changes in providers of distribution services; b. protection against fraudulent practices; and c. effective consumer education;
2. Establish effective mechanisms for energy service providers that ensure the security of payments made by energy service providers to utility distribution companies;
3. Provide validation and audit procedures necessary to ensure accurate and reliable metered data to support the commercial settlement process;

4. If cost credits to energy service providers are provided, require all of the cost credits to reflect the actual avoided costs of revenue cycle services on an individual customer basis (not the average cost), net of any additional costs incurred by the utility distribution company;
5. Provide for the full recovery of all investments and obligations incurred by the utility distribution company in providing services to customers prior to unbundling that may not be recoverable in rates as a result of unbundling of distribution services; and
6. Allow the utility distribution company to retain its meters, and to install interval metering at its discretion subject to regulatory approval.

Q5. Recently Chair Moller of the Federal Regulatory Commission recommended that, as part of comprehensive legislation, Congress authorize the Commission to enforce compliance with North American Electric Reliability Council standards to help maintain reliability of service. Do you believe this is necessary, and why or why not?

A5. Yes, while Edison believes that retail competition need not adversely affect reliability, we support changes that will enhance reliability. NERC is voluntary and there are no consequences for non-compliance with NERC standards. Furthermore, in a competitive market, reliability management will have to extend beyond utilities to generators, marketers, and transmission owners. Thus, a mandatory reliability management system is needed whereby all market participants are subject to a common set of "rules of the road". While state authority over reliability should be continued, we believe FERC should be given the power to enforce reliability requirements recommended by the council.

Q6. What concerns does your company have with respect to the role of public power and federal power marketing agencies in an increasingly competitive wholesale market? In markets in which retail competition has been adopted? Are there concerns you would like to have addressed if Congress enacts comprehensive restructuring legislation? Should Congress consider changes to federal law as it applies to regulation of public or federal power's transmission obligations?

A6. There cannot be a truly competitive market if some market participants have special provisions relative to tax and regulatory treatment. There are three broad areas where Congress needs to focus. First, publicly owned utilities should not be able, directly or indirectly, to sell to the retail customer of an investor-owned utility unless the public utility allows open access to its retail customers.

Second, Congress needs to ensure that the transmission lines of public power and federal power marketing agencies are subject to FERC's open access rules. Third, changes need to be made to the tax code to ensure a "level playing field." See Answer 7 below for specific recommendations.

An example of what's occurring in California can best demonstrate our concern. Last year, a provision was included in the Energy and Water appropriations bill to allow "excess" Bonneville Power Administration power to be sold outside the Northwest. It appears that much of this power is destined for the soon-to-be opened California market. Thus, companies like Edison will shortly be facing direct competition with subsidized federal power transmitted by an agency whose transmission lines are not subject to FERC's open access rules. There is nothing fair about this form of competition. Congress should eliminate the ability of federally subsidized power, such as that from BPA, to be sold into the competitive electricity market. If BPA power is to be sold outside the Northwest, it should at least be sold into a power exchange so that any cost benefits of that public power are provided to the broadest array of consumers.

Congress may consider allowing a local jurisdiction to opt out of the competitive market if it does not use its facilities to unfairly compete in the market or seek to serve customers in other jurisdictions, and only uses its tax-advantaged position to serve customers in its existing jurisdictional territory.

Q7. If Congress enacts comprehensive restructuring legislation, should changes be made to federal, state or local tax codes, and if so, why? Please be specific.

A7. In order to have a truly competitive market, Congress must make specific changes to the federal tax code. These changes include, but are not limited to:

1. Eliminating the ability of public power entities to issue new tax exempt debt for the purpose of expanding outside their traditional service territories; and
2. Eliminating the "two-county rule" which allows utilities with only two adjacent counties in their service territory to issue tax-exempt debt. This is specially relevant to Edison since there are three Western utilities that enjoy these benefits (SDG&E, Tucson, and Nevada Power).

The impact of electric restructuring on state and local taxes is a matter that is best left to the individual states. Each state is different and has different problems to deal with. For example, in California, property taxes, income taxes, and payroll taxes are the same for utilities as all other businesses. However, in other states,

special property tax rates and revenue taxes have been imposed on utilities that do not apply to other businesses. With the advent of retail competition, these tax structures may have to be restructured in order to avoid significant revenue losses. Resolving these problems will be unique to each state and locale. Accordingly, they should be left to states and local jurisdictions to fix.

Q8. What, if any, concerns do you have about the reliability of the electric system? If the industry moved to retail competition, will adequate reserves be available? If the transmission system capable of handling full retail competition?

A8. As stated above, Edison believes that retail competition need not adversely affect reliability. However, the shift away from the current system, in which utilities have exclusive retail franchises with the correlative obligation to serve all needs in that franchise area, to a system in which all customers can choose their supplier raises a number of important issues that must be addressed.

- First, an organization must be empowered to set mandatory “rules of the road” applicable to all participants in the electric industry with sanctions for non-compliance. This organization must be able to monitor and enforce compliance with its rules. NERC may be able to serve this role, with enforcement by the FERC, as discussed in response to question 5, above. Other options could also work;
- Second, it must be clear who is accountable for reliability. Under AB 1890 (the California restructuring law), for example, the Independent System Operator is responsible for ensuring reliable operation of the transmission system, including the procurement and maintenance of adequate generation reserves to provide voltage support, spinning reserves, etc. The utility distribution companies will be responsible for the safe and reliable delivery of power and will provide open, non-discriminatory access to their transmission and distribution systems. When accountability for reliability functions is not clearly defined, no participant in the system will have the incentive or the requirement to provide that service, and reliability inevitably will suffer. Edison believes that the Independent System Operator and utility distribution companies, operating in tandem in the competitive generation market, will ensure that adequate reserves will be available;
- Third, all market participants should be subject to mandatory reliability management rules and be subject to consequences for non-compliance;

- Fourth, all market participants must pay for the cost of maintaining grid reliability including the development, implementation, and operation of a mandatory reliability management system. The management responsibility for reliability should be vested with reliability councils (NERC/WSCC), Independent System Operators, or other appropriate institutions; and
- Fifth, there must be full compensation for the provision of reliability services. The market will develop to provide back-up power, for example, but only if market participants are required to pay for this when it is needed, rather than merely falling back on the utility distribution system as a supplier of last resort. This may be an option if the utility is compensated for it. What matters is that those who would supply retail customers provide all that is necessary to get that power to that customer (including ancillary services), or be obligated to compensate others for those services. In some retail pilot programs, for example, the utility has been forced to provide generation support and back-up power to maintain reliable service when third-party suppliers provided only the power that was promised to the customer, not the power necessary to maintain voltage support, spinning reserves, etc. The bottom line is that to ensure the reliability of the nation's electric system, suppliers of reliability services, be they utilities or other power producers, must be properly compensated.