TENNESSEE VALLEY AUTHORITY RESTRUCTURING

BRIEFING BOOK

January 28, 2000
Washington, DC
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OVERVIEW OF THE NEED FOR
TVA RESTRUCTURING LEGISLATION

In 1992, Congress made wholesale electric competition possible with the passage of the Energy Policy Act, legislation that was designed to remove the barriers to wholesale competition in the electric industry. Subsequent policy initiatives by the Federal Energy Regulatory Commission ("FERC"), including Order No. 888, further facilitated and encouraged the development of a nationwide competitive bulk power market. Wholesale electric competition is now a reality almost everywhere in the United States, with the exception of the Tennessee Valley region, where the Tennessee Valley Authority ("TVA"), the largest electric utility in the United States, continues to operate as a self-regulated monopoly.

Under existing law, TVA is the exclusive supplier of power within its statutorily defined service territory, an 80,000 square-mile area that includes virtually the entire state of Tennessee and parts of Kentucky, Mississippi, Alabama, Georgia, North Carolina, and Virginia. TVA is not permitted to sell power outside its service area, but it is also not required to transmit power from other suppliers to its customers inside the Valley. Nor are TVA's rates subject to review. As a result, TVA's customers are "captive" customers in the truest sense of the word; they have no opportunity to challenge TVA's rates before an independent regulator, they cannot choose to purchase power from a supplier other than TVA, and they have virtually no bargaining power with which to influence TVA's services or business practices.

Congress should act now to extend the benefits of wholesale competition to the residents of the Tennessee Valley. One of the obvious benefits of competition is downward pressure on rates. Outside the Valley, wholesale competition has already yielded lower prices. In Kentucky, for example, the wholesale rates charged by FERC-regulated utilities decreased significantly over the past several years, while TVA's wholesale rates increased by 7.5% systemwide. As a result, TVA's captive ratepayers in Kentucky will pay $250 million more for their power over the next five years than will Kentucky customers of Kentucky Utilities, a FERC-regulated investor-owned utility. The competitive pressures brought to bear by market forces have also encouraged efficiencies in operations and administration and innovations in marketing and technology throughout the industry. In fact, the success of wholesale competition thus far recently led the FERC to issue a rule on Regional Transmission Organizations designed to encourage competition at the wholesale level even further.

Yet, due to existing statutory and commercial barriers, there will never be wholesale electric competition in the Tennessee Valley unless Congress takes action. Only Congress has the power to introduce wholesale competition to the Tennessee Valley; FERC cannot do it, the States cannot do it, and the marketplace
cannot do it – because federal law prohibits it. It simply will not happen until Congress acts affirmatively to make it possible.

Because nationwide electric restructuring is a daunting task, there are those who say retail competition is already taking hold through the efforts of individual States, and that it will gradually spread across the country even if this Congress does nothing. Accordingly, many conclude that doing nothing in Congress is the best approach, at least for the time being. However, there is a huge difference between taking this wait-and-see approach for the rest of the country and taking it for TVA. The question in the Tennessee Valley is not whether to implement retail competition, but whether the Valley should be opened to wholesale competition, which the rest of the country has enjoyed since 1992. If Congress does nothing, many States will continue to move forward with retail competition, but the existing wholesale market will continue to evolve, too. As a result, if Congress does nothing, the rest of the country will continue to move forward – and the Tennessee Valley will be left behind.

If the Valley is ever really going to "catch up" with the rest of the country, Congress must act, and it must act now. To open the Valley to competition, Congress has to make some changes to TVA and the way it does business. First, the statutory barriers to competition in the Valley must be repealed. Second, TVA cannot continue to be self-regulated once the Valley is opened to competition. Instead, TVA should be subject to the same degree of regulatory oversight applicable to other utilities competing in the wholesale marketplace. In particular, FERC should have jurisdiction over TVA transmission, wholesale power sales, and stranded costs. Third, TVA must be subject to the antitrust laws to the same extent as other governmental entities. Other changes would also be necessary to ensure a smooth transition to competition in the Tennessee Valley. The various changes that are necessary, and the reasons why they are necessary, are set forth in the legislation that follows.
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<thead>
<tr>
<th>ISSUE</th>
<th>EXISTING LAW</th>
<th>H.R. 2950</th>
<th>S. 1847</th>
<th>H.R. 3064</th>
<th>S. 1513</th>
<th>H.R. 3172</th>
<th>S. 1572</th>
<th>S. ___</th>
<th>KUMLUW PROPOSAL</th>
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<tr>
<td>TVA LEGAL STATUS</td>
<td>Under the FPA &amp; PURPA, TVA is a: 1. Transmitting Utility (16 U.S.C. Sec. 796(b)) 2. Nonregulated Electric Utility (16 U.S.C. Sec. 3802(a)) 3. State Regulatory Authority (16 U.S.C. Sec. 7962(e) &amp; Sec. 7968(a)) TVA is not a Public Utility (16 U.S.C. Sec. 3246(d)).</td>
<td>Sec. 401(a) expressly repeals TVA's status as a state regulatory authority. Sec. 401(b) gives FERC jurisdiction over the TVA transmission system. Sec. 402(a) gives FERC jurisdiction over wholesale sales outside, but not inside, the Tennessee Valley region.</td>
<td>Sec. 601(g) expressly repeals TVA's status as a state regulatory authority. Sec. 601(b) gives FERC jurisdiction over the TVA transmission system. Sec. 601(c) gives FERC jurisdiction over wholesale sales outside, but not inside, the Tennessee Valley region.</td>
<td>Sec. 201 amends the TVA Act to provide that TVA shall be considered a &quot;public utility&quot; within the meaning of the PPA.</td>
<td>Sec. 301 amends the PPA definition of &quot;public utility&quot; to include TVA, &quot;but only with respect to determining, fixing, and otherwise regulating the rates, terms and conditions for the transmission of electrical energy to interstate customers&quot; under PPA Part II.</td>
<td>Sec. 101 amends PPA definition of &quot;public utility&quot; to include TVA, &quot;but only with respect to determining, fixing, and otherwise regulating the rates, terms and conditions for the transmission of electrical energy to interstate customers&quot; under PPA Part II.</td>
<td>Repeals TVA's status as a state regulatory authority. Gives FERC the same FPA jurisdiction over TVA transmission rates, terms, and conditions that applies to public utilities.</td>
<td>Subjects TVA to FERC jurisdiction over wholesale sales and stranded costs.</td>
<td></td>
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| WHOLESALE TRANSMISSION ACCESS | FERC may order TVA to transmit the power of other utilities if it would be consumed within TVA's service area (i.e., within the TVA service). (16 U.S.C. Sec. 324; 824(b)). TVA may not grant nonpublic transmission access to public utilities from which it receives transmission service (FERC Order 600). | Sec. 600(a) makes most of Parts II and III of the PPA (and FERC's regulations and policies promulgated thereunder) applicable to TVA's transmission facilities and transmission of electric energy and the provision of necessary ancillary services over the TVA transmission system, except that FERC determinations pursuant to such provisions apply to public utilities. | Sec. 600 makes most of Parts II and III of the PPA (and FERC's regulations and policies promulgated thereunder) applicable to TVA's transmission facilities and provide for the transmission of electric energy and the provision of necessary ancillary services over the TVA transmission system, except that FERC determinations pursuant to such provisions apply to public utilities. | Sec. 601(a) defines TVA as a public utility, open access requirements of FERC Order No. 688 would be applicable to TVA. However, without repeal of the anti-cherry-picking provision, FERC cannot mandate open access to the TVA transmission system where the power to be transmitted would be consumed within the Fense. | Sec. 601(a) subjects TVA transmission system to FERC jurisdiction; open access requirements of FERC Order No. 688 would be applicable to TVA. However, without repeal of the anti-cherry-picking provision, FERC cannot mandate open access to the TVA transmission system where the power to be transmitted would be consumed within the Fense. | Sec. 101 subjects TVA transmission system to FERC jurisdiction; open access requirements of FERC Order No. 688 would be applicable to TVA. However, without repeal of the anti-cherry-picking provision, FERC cannot mandate open access to the TVA transmission system where the power to be transmitted would be consumed within the Fense. | Subjects TVA's transmission rate, terms and conditions to FERC jurisdiction, including the open access requirements of FERC Order No. 688. |

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Obtained and made public by the Natural Resources Defense Council, March/April 2002
<table>
<thead>
<tr>
<th>ISSUE</th>
<th>EXISTING LAW</th>
<th>H.R. 2310 (SARGENT, MARKET)</th>
<th>S. 1047 (SIMPSON)</th>
<th>H.R. 2944 (COMMITTEE PRINT)</th>
<th>S. 1225 (MCCONNELL)</th>
<th>H.R. 2128 (HARGAMAN)</th>
<th>S. 1172 (MURKOWSKI)</th>
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<tr>
<td>ANTICHERY PICKING PROVISION</td>
<td>FPA sec. 212(j) mandates that FERC cannot exempt TVA from transmission service to another entity if the power will be consumed within the TVA Fence (16 U.S.C. Sec. 824a(j))</td>
<td>Explicitly repealed by Sec. 4051(b)(3).</td>
<td>Explicitly repealed by Section 607(d).</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Explicitly repealed. Wholesale electric competition in the Tennessee Valley will never be possible unless and until this provision is repealed.</td>
</tr>
<tr>
<td>THE FENCE</td>
<td>Sec. 211(b) of FPA and Sec 164(b) of TVA Act prevent TVA from making contracts beyond the effect of making TVA or the distribution a source of power supply outside the Fence (16 U.S.C. Sec. 824(a), 48.566-641).</td>
<td>Explicitly repealed by Sec. 4051(b). Sec. 4051(b) specifically authorizes TVA to sell power as wholesale to any person as of 01/01/2003.</td>
<td>Explicitly repealed by Sec. 4052(a) &amp; 4052(b). Sec. 4052(a) limits TVA wholesale power sales for use outside the Tennessee Valley to &quot;non electric energy.&quot;</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Explicitly repealed. Wholesale electric competition in the Tennessee Valley will never be possible unless and until these provisions are repealed.</td>
</tr>
<tr>
<td>REVIEW OF TVA TRANSMISSION RATES</td>
<td>None.</td>
<td>Sec. 403(a) gives FERC the same FPA authority over TVA transmission rates, terms and conditions as over any public utility.</td>
<td>Sec. 807 gives FERC the same FPA authority over TVA transmission rates, terms and conditions as over any public utility.</td>
<td>Sec. 807 gives FERC the same FPA authority over TVA transmission rates, terms and conditions as over any public utility.</td>
<td>Sec. 6(a), which makes TVA a public utility, gives FERC authority over TVA transmission rates, terms and conditions.</td>
<td>Sec. 6(a), which makes TVA a public utility, gives FERC authority over TVA transmission rates, terms and conditions.</td>
<td>Sec. 151 gives FERC authority over TVA's transmission rates, terms and conditions.</td>
<td>Applies FERC jurisdiction to TVA's transmission rates to the same extent that such jurisdiction applies to public utilities.</td>
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<tr>
<th>ISSUE</th>
<th>EXISTING LAW</th>
<th>H.R. 2150 (CANDLER, MARKERT)</th>
<th>S. 1547 (H.R. 2124) (COMMITTEE PRINTS)</th>
<th>H.R. 3325 (McConnell)</th>
<th>H.R. 2150 (BAKER)</th>
<th>S. 1579 (BINGHAMAN)</th>
<th>S. 1538 (MURKOWSKI)</th>
<th>KUBELLOW PROPOSAL</th>
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<tbody>
<tr>
<td>REVIEW OF TVA WHOLESALE POWER RATES</td>
<td>None.</td>
<td>Sec. 412(c) gives FERC authority to review TVA wholesale power rates.</td>
<td>Not addressed.</td>
<td>Sec. 412(c) gives FERC authority to review TVA wholesale power rates.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Gives FERC FPA jurisdiction over rates, terms and conditions of TVA wholesale power rates. TVA should be subject to same FERC authority to regulate wholesale power rates that applies to public utilities. If so, TVA could pre-recover uncollectible stranded costs or otherwise circumvent FERC Order 888 stranded cost recovery principles.</td>
</tr>
<tr>
<td>WHOLESALE STRANDED COST RECOVERY BY TVA</td>
<td>None, absent triggering of FERC Order 888 stranded cost recovery by TVA</td>
<td>Sec. 605 direct FERC to promulgate regulations governing stranded cost recovery by TVA and to employ a methodology consistent with that used by FERC in determining public utility stranded costs. No stranded cost charge may be imposed after 8/30/2007.</td>
<td>Sec. 605 directs FERC to promulgate regulations governing stranded cost recovery by TVA.</td>
<td>Sec. 605 directs FERC to promulgate regulations governing stranded cost recovery by TVA.</td>
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FERC, the federal body with the most significant expertise in this regard, has already struggled with the issue of how best to deal with costs "stranded" as a result of the transition to competition in the electric industry. Order No. 888 reprimands FERC's conclusions as to the most fair and efficient mechanism for calculating and assessing stranded costs. There is no reason for departing from this mechanism when determining TVA's stranded costs.
<table>
<thead>
<tr>
<th>ISSUE</th>
<th>EXISTING LAW</th>
<th>H.R. 8000 (GAGE, MARKER)</th>
<th>S. 1847 (H. R. 1835) (ADMINISTRATION)</th>
<th>H.R. 3094 (COMMITTEE PRINT)</th>
<th>S. 1383 (McCONNELL)</th>
<th>H.R. 3120 (BAKER) (HIGGINS)</th>
<th>S. 1778 (MURKOWSKI)</th>
<th>KUHL/MURKOWSKI PROPOSAL</th>
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<tbody>
<tr>
<td>REFORM OF LONG-TERM TVA CONTRACTS WITH DISTRIBUTORS</td>
<td>None</td>
<td>Sec. 601 requires TVA to renegotiate its existing long-term distribution contracts within one year of enactment, including provisions with respect to term, termination notice, purchase from other suppliers, and stranded cost recovery. Upon expiration of the one-year period, any remaining issues would be submitted to FESC for final resolution.</td>
<td>Sec. 608 requires TVA to renegotiate its existing long-term distribution contracts within one year of enactment, including provisions with respect to term, termination notice, purchase from other suppliers, and stranded cost recovery. Upon expiration of the one-year period, any remaining issues would be submitted to FESC for final resolution.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Allows distributors to terminate or reduce purchases under existing contracts with TVA on two years’ notice.</td>
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KUHLMURKOWSKI long-term TVA contracts were entered into under entirely different regulatory regime and with vastly disparate bargaining power. These contracts renew automatically each year and require 180 days’ notice of termination. Congress should modify these contracts to shorten the length of notice for termination. A two-year notice period would be less costly and provide distributors with meaningful bargaining power in negotiations for replacement contracts and Bafford sufficient time for TVA to market the power no longer purchased by distributors giving notice of termination.

REGULATORY AUTHORITY BY TVA OVER DISTRIBUTORS | TVA Act Secs. 10 & 12 allow TVA to exercise regulatory authority over distribution through power supply contracts (16 U.S.C. Sec. 833, 811). | Sec. 407(c) allows distributors to opt out of regulation by TVA. Upon a distributor’s election, the provisions of Secs. 10 and 12 of the TVA Act that allow TVA to regulate distributors through power supply contracts will not apply to future sales by TVA to that distributor. | Sec. 507(2) specifically repeals the provisions of Secs. 10 and 12 of the TVA Act that allow TVA to regulate distributors through power supply contracts. | Not addressed. | Not addressed. | Not addressed. | Not addressed. | Terminates regulation of distributors by TVA and transfers regulatory authority to state or local governing bodies. Any general matter, it is inappropriate in a competitive market, for a wholesale supplier to regulate a retail distributor.
<table>
<thead>
<tr>
<th>ISSUE</th>
<th>EXISTING LAW</th>
<th>H.R. 3196 (CLAGGENT-MARKET)</th>
<th>H.R. 1947 (S. 1936 - ADMINISTRATION)</th>
<th>H.R. 3084 (COMMITTEE PRINT)</th>
<th>S. 1832 (MACONWELL)</th>
<th>H.R. 3196 (HARKER)</th>
<th>S. 1573 (RINGAAMAN)</th>
<th>KERINLOW PROPOSAL</th>
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</thead>
<tbody>
<tr>
<td>ANTIETRUST</td>
<td>Not addressed.</td>
<td>Sec. 402 makes the federal antitrust laws applicable to TVA but insulates TVA from civil damages liability for antitrust violations.</td>
<td>Sec. 603 makes the federal antitrust laws applicable to TVA but insulates TVA from civil damages liability for antitrust violations.</td>
<td>Sec. 603 makes the federal antitrust laws applicable to TVA but insulates TVA from civil damages liability for antitrust violations.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Makes the federal antitrust laws applicable to TVA but insulates TVA from civil damages liability for violations. Because TVA is a governmental entity, damages for antitrust violations would ultimately be borne by taxpayers. Thus, TVA should enjoy the same immunity as other governmental entities.</td>
</tr>
<tr>
<td>RETAIL SALES</td>
<td>The Fene prohibits TVA from selling power at retail or wholesale outside the Valley. Yet the statute limits TVA’s ability to make retail sales outside the Valley, but TVA’s customers with its distributors prevent TVA from competing with them for retail customers.</td>
<td>Sec. 602(a) authorizes TVA to make certain retail sales outside, but not inside, the Fene. Sec. 603(a) authorizes TVA to make retail sales and existing retail customers to retail customers within a distributor’s service area if the distributor: (1) consents to the sale; or (2) purchases more than 65 percent of its power from a supplier other than TVA.</td>
<td>Permits TVA to make certain retail sales inside, but not outside, the Fene. Sec. 602(a) authorizes TVA to make retail sales to existing retail customers within a distributor’s service area if the distributor: (1) consents to the sale; or (2) purchases more than 65 percent of its power from a supplier other than TVA.</td>
<td>Permits TVA to make certain retail sales outside, but not inside, the Fene. Sec. 602(a) authorizes TVA to make retail sales to existing retail customers within a distributor’s service area if the distributor: (1) consents to the sale; or (2) purchases more than 65 percent of its power from a supplier other than TVA.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Authorizes TVA retail sales to existing TVA retail customers and those within a distributor’s service area if the distributor consents.</td>
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<tr>
<td>WHOLESALE SALES OUTSIDE THE VALLEY</td>
<td>The TVA Act permits TVA, subject to certain restrictions, to sell outside the Fene within an area extending not more than five miles beyond the Fene. 16 U.S.C. § 831 et seq.</td>
<td>Sec. 634 permits TVA to sell power at wholesale to any person outside the Tennessee Valley in “normative economic sense.”</td>
<td>Sec. 602(b)(2) permits TVA to sell power at wholesale outside the Valley, but limits TVA power sales for use outside the Tennessee Valley to “normative economic power.”</td>
<td>Sec. 602(b)(2) permits TVA to sell power at wholesale to “any person” as of January 1, 2003.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not specifically addressed, but KERINLOW support permitting TVA to sell wholesale electricity outside the Valley. TVA’s participation in competitive markets should not be restrained unnecessarily, especially whereany revenues generated by any TVA power sales will mitigate TVA’s stranded costs.</td>
</tr>
<tr>
<td>Issuer</td>
<td>Existing Law</td>
<td>S. 1880 (GARGAINT MARKET)</td>
<td>H.R. 2504 (ADMINISTRATION)</td>
<td>S. 1223 (McCONNELL)</td>
<td>H.R. 2156 (BAKER)</td>
<td>S. 2473 (MURKOWSKI)</td>
<td>Kuusalo Proposal</td>
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<td>New Generation Capacity</td>
<td>Sec. 404 of the TVA Act authorizes TVA to &quot;purchase or lease&quot; such real property as it deems necessary or convenient in the transaction of its business.&quot; 16 U.S.C. § 834(d). Sec. 5 of the TVA Act authorizes the TVA Board to &quot;make alterations, modifications, or improvements to existing plants and facilities, and to construct new plants.&quot; 16 U.S.C. § 813(d). Sec. 18 and 19 of the TVA Act authorize TVA to issue bonds to finance, among other things, the construction, acquisition, enlargement, improvement, or replacement of power-generating plants. 16 U.S.C. § 813m &amp; 813n-1.</td>
<td>Sec. 404 prohibits TVA from acquiring new generating resources unless the customer on whose behalf the resource is acquired is required to bear the cost of acquisition. Sec. 404 further provides that TVA must consent to the use of new generating resources that would otherwise be in excess of the customer's demand.</td>
<td>Sec. 5(a) prohibits TVA from constructing or acquiring any additional generation capacity unless FERC issues a certificate of public convenience and necessity authorizing construction or generation. Sec. 5(a) further provides that FERC's issuance of such certificate is to cease unless the following conditions are met: (1) the new resource is completely subscribed in advance by the distributor; (2) the new resource is not expected to increase TVA's stranded cost; (3) the new resource is not expected to increase TVA's stranded cost; (4) the new resource is not expected to increase TVA's stranded cost.</td>
<td>Sec. 5(a) prohibits TVA from constructing or acquiring any additional generation capacity unless FERC issues a certificate of public convenience and necessity authorizing construction or generation. Sec. 5(a) further provides that FERC's issuance of such certificate is to cease unless the following conditions are met: (1) the new resource is completely subscribed in advance by the distributor; (2) the new resource is not expected to increase TVA's stranded cost; (3) the new resource is not expected to increase TVA's stranded cost; (4) the new resource is not expected to increase TVA's stranded cost.</td>
<td>Not addressed.</td>
<td>Not addressed.</td>
<td>Not specifically addressed. Kuusalo opposes excessive statutory limitations on TVA's ability to construct or acquire new generation facilities, which would interfere with TVA's ability to meet the customers' demand. However, TVA would not need to build new generation facilities if TVA would permit its customers to provide for their own load growth, whether by generating power or by purchasing power from other suppliers on the wholesale market. Neither of these options is barred by existing law, but both would probably require the approval of FERC. First, TVA would likely argue that the distributor's TVA constructs prohibit self-generation. Second, unless or until the anti-cherry-picking provision is repealed, purchases from other suppliers would require that TVA unilaterally provide access to its transmission system for transmitting power to wholesale generators. FERC, TVA is not likely to agree to provide this access unless or until the FERC is reminded, perhaps giving TVA arm's-length access to market power outside the Tennessee Valley.</td>
<td></td>
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</table>
SEC. 1  DEFINITIONS.

Except as otherwise expressly provided, the following definitions shall apply for the purposes of this title:

(a) DISTRIBUTOR — The term “distributor” means a cooperative organization, municipal, or other publicly owned electric power system (or any successor in interest thereto) which on January 2, 1998, purchased substantially all of its wholesale power requirements at wholesale from TVA pursuant to a long-term power sales agreement.

(b) TENNESSEE VALLEY — The term “Tennessee Valley” means the geographic area in which TVA was providing wholesale power to distributors on January 2, 1998.

(c) TVA — The term “TVA” means the Tennessee Valley Authority.

(d) COMMISSION -- The term "Commission" means the Federal Energy Regulatory Commission or any successor agency.

SEC. 2  REMOVAL OF RESTRICTIONS ON ELECTRIC ENERGY SALES BY TVA AND ITS DISTRIBUTORS OUTSIDE OF THE TVA SERVICE AREA.

The first paragraph, from the beginning of the third sentence through the end, the second paragraph, and the third paragraph of Section 15d(a) of the Tennessee Valley Authority Act of 1933 (16 U.S.C. § 831n-4(a)) are repealed.

SEC. 3  OPEN ACCESS TRANSMISSION BY TVA.

(a) The rates, terms, and conditions of transmission service provided by TVA shall be regulated by and under the jurisdiction of the Commission in the same manner and to the same extent as the rates, terms, and conditions of transmission service provided by all transmission owners and/or operators, provided that the preference granted in Section 10 of the Tennessee Valley Authority Act (16 U.S.C. § 831i) to States, counties, municipalities, and cooperative organizations of citizens or farmers within the Tennessee Valley shall include access to transmission capacity on the TVA transmission system.
SEC. 7  POWER SALES BY TVA.

(a) Nothing in this title shall be construed to modify or alter the existing obligations of TVA under the Tennessee Valley Authority Act (16 U.S.C. § 831 et seq.) to give preference in the sale of power to States, counties, municipalities, and cooperative organizations of citizens or farmers within the Tennessee Valley.

(b) No person or entity shall duplicate the facilities of a distributor for the purpose of serving a retail customer. TVA shall not deliver power to retail customers without the consent of the distributor that would otherwise provide distribution service to such customer, provided that TVA may continue to make those retail sales it was making on the date of enactment, provided that distributors retain all their rights to pursue any legal claims they may have that a retail sale being made by TVA on the date of enactment violated applicable provisions of law or contracts.

SEC. 8  EXISTING WHOLESALE POWER CONTRACTS.

(a) DISTRIBUTOR CONTRACT TERMINATION OR REDUCTION RIGHT.--- TVA shall allow any distributor that had a contract to purchase wholesale electric energy from TVA in effect on the date of enactment of this title to terminate its contract or reduce the quantity of its wholesale power requirements thereunder by or to either a specific amount of power or a percentage of its requirements, upon two years' notice, which notice may be given at any time and from time to time from the date of enactment.

(b) RENEGOTIATION OF CERTAIN WHOLESALE POWER CONTRACTS.--- If a distributor elects to reduce the quantity of its purchases from TVA pursuant to subsection (a) of this Section 8 but not to terminate its contract, such distributor and TVA shall, within one year following the date of such election, renegotiate the remaining terms of their existing contract under which TVA will continue to provide wholesale power to the distributor, provided that such contract shall preserve the distributor's right under subsection (a) to elect further reduction(s). If the distributor and TVA are not able to reach agreement on such remaining terms of their contract within the one-year period, either the distributor or TVA may submit the matter to the Commission which shall have jurisdiction to and shall establish such terms.

SEC. 9  RECOVERY OF STRANDED COSTS.

TVA may recover any wholesale stranded costs that may arise from the exercise of rights by a distributor pursuant to Section 8 of this title to the extent authorized by the Commission based on application of the same rules and principles the Commission applies to wholesale stranded cost recovery by other electric utilities within its jurisdiction, provided that TVA shall not be authorized to recover
from any distributor any wholesale stranded costs related to loss of sales or
revenues by TVA, or its expectation of continuing to sell electric energy, for any
period after September 30, 2007. Any stranded cost recovery charge authorized by
the Commission to be assessed by TVA shall be unbundled from the otherwise
applicable rates and charges to such customer and separately stated on the bill of
such customer. TVA shall not recover wholesale stranded costs from any customer
through any other rate, charge, or mechanism.
SECTION ONE: DEFINITIONS

Proposed Legislative Language:

SEC. 1 DEFINITIONS.

Except as otherwise expressly provided, the following definitions shall apply for the purposes of this title:

(a) DISTRIBUTOR – The term "distributor" means a cooperative organization, municipal, or other publicly owned electric power system (or any successor in interest thereto) which on January 2, 1998, purchased substantially all of its wholesale power requirements at wholesale from TVA pursuant to a long-term power sales agreement.

(b) TENNESSEE VALLEY – The term "Tennessee Valley" means the geographic area in which TVA was providing wholesale power to distributors on January 2, 1998.

(c) TVA – The term "TVA" means the Tennessee Valley Authority.

(d) COMMISSION -- The term "Commission" means the Federal Energy Regulatory Commission or any successor agency.

Rationale:

In the interest of clarity and brevity, this section defines several of the terms or abbreviations used throughout the title.

The term "distributor," as used in the title, refers to a member of a particular class of TVA customers. TVA sells power to two different classes of customers in the Tennessee Valley: (1) end-use retail customers directly served by TVA; and (2) wholesale distributors that re-sell TVA power to their own retail customers. At present, there are 159 "distributors" of TVA power, all of which are publicly-owned, not-for-profit electric distribution systems. Section 1(a) defines the term "distributor" so as to include all 159 distributors, including electric cooperatives as well as municipal electric systems, to the exclusion of all other TVA customers.

The term "Tennessee Valley," as used in the title, refers to the geographic area within which TVA is permitted to sell power under existing law. The 1959 amendments to the TVA Act generally restricted TVA's service territory to the geographic area it was serving on July 1, 1957. See 16 U.S.C. § 831n-4(a). This territorial restriction is commonly referred to as the "TVA Fence" (or simply the

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"Fence"). As used in the TVA title, the term "Tennessee Valley" means the geographic area bounded by the Fence.

As used in this title, the "Commission" means the Federal Energy Regulatory Commission ("FERC"). The FERC is the federal agency with regulatory authority over, among other things, natural gas and electric utilities operating in interstate commerce.
SECTION TWO: THE TVA FENCE

Proposed Legislative Language:

SEC. 2 REMOVAL OF RESTRICTIONS ON ELECTRIC ENERGY SALES BY TVA AND ITS DISTRIBUTORS OUTSIDE OF THE TVA SERVICE AREA.

The first paragraph, from the beginning of the third sentence through the end, the second paragraph, and the third paragraph of Section 15d(a) of the Tennessee Valley Authority Act of 1933 (16 U.S.C. § 831n-4(a)) are repealed.

Background:

Before 1959, there were no statutory barriers limiting TVA power sales to any particular region. Pursuant to the TVA Act, TVA’s primary purpose was (and still is) to serve the Tennessee Valley region, see 16 U.S.C. § 831, but TVA was technically free to sell electricity anywhere in the U.S. See Alabama Power Co. v. TVA, 948 F. Supp. 1010, 1023 (N.D. Ala. 1996). However, the 1959 amendments to the TVA Act restricted TVA power sales to a defined geographic area. See 16 U.S.C. § 831n-4(a). Section 15d(a) of the TVA Act generally prohibits TVA from selling or delivering power, directly or indirectly, outside the geographic area within which it was the primary source of power on July 1, 1957. See id. This statutory provision is known as the “TVA Fence” because it “fences” TVA in, limiting TVA power sales to a defined service area.

The primary purpose of the Fence was to protect private utilities from TVA competition. See Hardin v. Kentucky Utilities Company, 390 U.S. 1, 7 (1968). Prior to the 1959 amendments to the TVA Act, TVA had been dependent on annual appropriations from Congress to finance capital expenditures for its power program. In the mid-1950s, however, TVA began to seek authority to issue bonds to finance such expenditures. Although TVA assured Congress at the time that its objective was not to expand its territory but to improve facilities within its existing service area, many Members of Congress were skeptical of TVA’s professed intentions. They insisted that legislation giving TVA bond authority should also include some mechanism aimed at preventing TVA from expanding its territory. In the late 1950s, several bills combining the grant of borrowing power with provisions prohibiting territorial expansion were introduced in Congress. One of these bills was ultimately enacted as the 1959 amendments to the TVA Act.
Rationale:

Section 2 repeals the TVA Fence, thereby permitting TVA to sell power outside the Tennessee Valley. Repeal of the Fence is necessary if the Valley is to be opened to competition. In fairness, if other suppliers are to be permitted to compete with TVA inside the Tennessee Valley, then TVA should be permitted to compete outside the Fence. In addition, permitting TVA to sell power outside the Fence will enable TVA to mitigate stranded costs that could result from the transition to wholesale competition in the Tennessee Valley.

For these reasons, TVA, TVPPA, Knoxville Utilities Board (“KUB”), and Memphis Light, Gas and Water Division (“MLGW”) all support legislation repealing the TVA Fence. TVA Watch, however, generally opposes repeal of the Fence, at least until such time as TVA Watch is satisfied that TVA would be competing with its members and other investor-owned utilities (IOUs) on a “level playing field.” TVA Watch is particularly concerned about TVA’s unique status as a wholly unregulated entity operating in interstate commerce. TVA Watch argues that TVA enjoys artificial competitive advantages—including exemptions from antitrust laws, FERC regulation, and state and local taxes—that would give TVA an unfair advantage in a competitive market.

Under the legislation, TVA would not enjoy an unfair competitive advantage over IOUs in the wholesale power market. In addition to repealing the Fence, the legislation subjects TVA to most of the laws that apply to public utilities. For example, the legislation provides for full FERC jurisdiction over TVA’s transmission, wholesale rates, and stranded costs. Section 5 of the legislation also subjects TVA to the antitrust laws to the same extent that such laws apply to other governmental entities. These measures assure that TVA will not have an unfair advantage over IOUs in the wholesale power market. Therefore, Tennessee Valley stakeholders do not advocate a simple repeal of the Fence in the absence of other changes to TVA and the way it does business. Instead, they support repeal of the Fence as one essential element of comprehensive TVA restructuring legislation.

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1 IOUs, as distinguished from “public power entities” such as TVA and the distributors, are for-profit entities owned by their shareholders.

2 See Section 3 (TVA Transmission).

3 See Section 4 (Regulation of TVA Wholesale Sales).

4 See Section 9 (Stranded Costs).

5 See Section 5 (Antitrust).
SECTION THREE: TVA TRANSMISSION

Proposed Legislative Language:

SEC. 3 OPEN ACCESS TRANSMISSION BY TVA.

(a) The rates, terms, and conditions of transmission service provided by TVA shall be regulated by and under the jurisdiction of the Commission in the same manner and to the same extent as the rates, terms, and conditions of transmission service provided by all transmission owners and/or operators, provided that the preference granted in Section 10 of the Tennessee Valley Authority Act (16 U.S.C. § 831i) to States, counties, municipalities, and cooperative organizations of citizens or farmers within the Tennessee Valley shall include access to transmission capacity on the TVA transmission system.

(b) Sections 219(f) and 219(g) of the Federal Power Act (16 U.S.C. §§ 824k(f) and 824k(j)) are repealed.

Background:

Transmission lines have been called "the highways of electricity commerce." Jeffrey D.Watkins & Douglas W. Smith, The Energy Policy Act of 1992—A Watershed for Competition in the Wholesale Power Market, 10 Yale J. on Reg. 447, 455 (1993). Without open access to transmission lines, a competitive bulk power market would not be possible. Therefore, provisions expanding FERC's authority over transmission were a fundamental feature of the Energy Policy Act of 1992 ("EPAct"), the omnibus energy legislation that "became the vehicle for addressing the obstacles to competition in the electric industry." Id.

Prior to the EPAct, access to transmission lines was controlled primarily by utilities that were also the dominant suppliers of electricity and that could retain their power and status in the market for electricity either by simply denying others access to their transmission lines or by offering access at rates that were so high as to be cost-prohibitive to competitors. In an effort to facilitate the development of a competitive wholesale market for the sale of electricity as a commodity, Congress in the EPAct increased FERC's authority over transmission owners and operators. The EPAct authorizes FERC to order transmitting utilities to provide transmission service to any electric utility (or other person or entity generating electric energy for sale for resale) requesting such service. See 16 U.S.C. § 824j. TVA is a "transmitting utility" within the meaning of the FPA and the EPAct's amendments thereto. See 16 U.S.C. § 796(23) (defining a "transmitting utility" as "any electric utility . . . or Federal power marketing agency which owns or operates electric power transmission facilities . . . for the sale of electric energy at wholesale"); 16
U.S.C. § 796(22)(expressly including TVA within the FPA definition of “electric utility”).

However, although the EPAct expanded FERC’s authority over TVA transmission, the legislation also included an important exception that seriously limits the extent of FERC’s power to order TVA to provide transmission service. See 16 U.S.C. § 824k(i). The exception is commonly referred to as the “anti-cherrypicking provision” because it prevents potential TVA competitors from selling power to customers inside the Fence (i.e., “cherrypicking”) without TVA’s consent. Specifically, the anti-cherrypicking provision provides that FERC may not issue an order requiring TVA to provide transmission service to another entity if the electricity to be transmitted would be consumed within the Fence. Therefore, pursuant to the EPAct, FERC has the power to order TVA to transmit power of other suppliers through—but not into—the Tennessee Valley. As a result, under existing law, power suppliers other than TVA could reach customers inside the Tennessee Valley (where TVA owns virtually 100% of the transmission lines) only if TVA were to voluntarily agree to provide the necessary access to its transmission system. To date, TVA has shown no willingness to volunteer to provide such access.

Rationale:

TVA and all the distributors support legislation that repeals the anti-cherrypicking provision and brings TVA transmission under FERC jurisdiction. Section 3(a) gives FERC regulatory authority over the rates, terms and conditions of TVA transmission service, while Section 3(b) repeals the anti-cherrypicking provision. By repealing the anti-cherrypicking provision, Section 3 gives FERC the authority to order TVA to provide transmission service to power suppliers seeking to use TVA’s transmission lines for the purpose of delivering power to wholesale customers inside the Valley. Section 3 also specifically provides for FERC jurisdiction over TVA transmission because under existing law, FERC does not have general jurisdiction over TVA’s transmission rates or the terms and conditions of TVA transmission service. FERC jurisdiction will ensure the smooth and fair operation of the TVA transmission grid, thereby promoting the development of an efficient bulk power market in the southeastern United States.

Section 3(a) further clarifies that the TVA Act’s preference provision extends to capacity on the TVA transmission system as well as to TVA’s power supply. Section 10 of the TVA Act provides that TVA shall give preference in the sale of power to “States, counties, municipalities, and cooperative organizations of citizens or farmers, not organized or doing business for profit, but primarily for the purpose of supplying electricity to its own citizens or members.” 16 U.S.C. § 831i. Absent this clarification, not-for-profit distributors choosing to purchase their power from a supplier other than TVA might be denied access to TVA’s available transmission capacity. This clarification is therefore necessary to remove any disincentive that
TVA might otherwise have, when allocating its available transmission capacity, to prefer customers that continue purchasing their power from TVA over those seeking to take advantage of competitive market opportunities by purchasing from other power suppliers.
SECTION FOUR: REGULATION OF TVA WHOLESALE SALES

Proposed Legislative Language:

SEC. 4 REGULATION OF SALES OF ELECTRIC ENERGY AT WHOLESALE BY TVA.

The rates, terms, and conditions of wholesale sales of electric energy by TVA shall be subject to the Federal Power Act (16 U.S.C. §§ 796 et seq.) and regulated by and under the jurisdiction of the Commission. All such rates shall be cost-justified unless the Commission finds that TVA possesses no market power in connection with a particular sale.

Background:

Under the FPA, FERC has jurisdiction over public utilities' wholesale power sales in interstate commerce, including the rates, terms, and conditions of such sales. See 16 U.S.C. 824d(a). In addition to providing that FERC has jurisdiction over wholesale sales of electricity, Section 205 of the FPA requires that the rates for such sales be just and reasonable and not unduly preferential or discriminatory. See 16 U.S.C. § 824d(a)-(b). Pursuant to FPA Section 205, public utilities subject to FERC jurisdiction must file with FERC all rates and contracts for the transmission or wholesale sale of power in interstate commerce. See 16 U.S.C. § 824d(c). In addition, public utilities must give FERC and the public at least 60 days' notice of any proposed rate increase. See 16 U.S.C. § 824d(d). Pursuant to the FPA, customers have the right, under section 206, to file a complaint with FERC challenging particular rates or contracts as unjust, unreasonable, or unduly discriminatory or preferential. See 16 U.S.C. §824e(a).

Unlike public utilities, TVA is not subject to any regulatory oversight under existing law. Instead, TVA is entirely self-regulated; its discretion to determine the rates, terms, and conditions of its wholesale sales of electric energy in interstate commerce is virtually unfettered. Under existing law, TVA answers only to Congress, a body that has neither the time nor the resources to devote to reviewing TVA's power rates. In addition, while congressional oversight theoretically affords TVA customers some protection from unjust, unreasonable, or unduly discriminatory power rates, there is simply no established procedure through which TVA customers could seek review of TVA's rates before Congress. In practice, congressional oversight of TVA is generally limited to budgetary issues.

Rationale:

Section 4 would bring TVA's wholesale sales under FERC jurisdiction. In a competitive market, it simply would not be appropriate for TVA to continue to set

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its own rates without any regulatory oversight. If TVA is going to be a market participant, then it should be subject to the same statutes, rules, and regulations that apply to other market participants of similar size, including sections 205 and 206 of the FPA. There is no sound public policy justification for exempting TVA from these provisions of the FPA.

It has been suggested by some that TVA's wholesale rates should merely be subject to judicial review in the federal district courts, or to compulsory arbitration proceedings in the event of a dispute. However, these are not viable alternatives to FERC regulation. Unlike state and federal courts and arbitration panels, which are ill-suited to the task of reviewing power rates, FERC has decades of expertise in regulating utilities' wholesale rates. In addition, FERC's many years of experience with wholesale rate regulation have produced a well-developed body of law to guide FERC in the exercise of its power. Thus, common sense and efficiency dictate that FERC, the entity best suited to the task, be given responsibility for reviewing, modifying, and approving TVA's wholesale rates.

It should be noted that the extent to which FERC regulates utilities' wholesale power rates is on the decline. FERC regulation of bulk power sales has become increasingly light-handed since the advent of wholesale competition. One consequence of the transition to competition in the electric industry has been increased reliance on market forces to accomplish what had, in the past, necessitated government regulation. Because open access to interstate transmission lines has largely dissipated most utilities' generation market power, FERC has granted many utilities' applications for authority to charge market-based rates. In the Tennessee Valley, however, TVA continues to have a monopoly on generation as well as transmission facilities. It is reasonable to believe that TVA's generation market power will recede over time, but protection from market power abuses by TVA will be particularly important during the early years of the transition to competition.

Absent oversight by a neutral body, TVA could use its market power to the detriment of customers inside the Valley. For example, TVA could increase wholesale rates for the purpose of cross-subsidizing other aspects of its power program, such as its transmission system. In addition, federal electric restructuring legislation giving FERC regulatory authority over certain aspects of TVA's power program but not over wholesale rates could seriously impair FERC's exercise of jurisdiction over TVA. For example, TVA has assented to limited FERC jurisdiction over its stranded costs, but such jurisdiction would be virtually meaningless unless FERC also has jurisdiction over TVA's wholesale rates as well. To illustrate, if TVA continues to have unfettered authority to set its wholesale rates, then TVA could circumvent FERC stranded cost determinations by increasing rates in the event of any perceived shortfall in FERC's stranded costs orders. To
prevent these and other potential abuses, TVA’s rates must be subject to review by FERC.

For all of the foregoing reasons, Section 4 gives FERC regulatory authority over the rates, terms, and conditions of TVA’s wholesale sales of electricity. Section 4 further requires that TVA’s rates be based on its cost of service unless or until FERC finds that TVA has no market power in connection with a particular sale. In essence, this language directs FERC not to grant TVA the authority to charge market-based rates until FERC determines that TVA no longer possesses market power.

TVA Position

The prospect of FERC regulation of TVA’s rates is anathema to TVA: TVA argues that there is no need for one body of presidential appointees (the FERC Commissioners) to review the rates set by another group of presidential appointees (the TVA Board). This argument, however, is flawed in several respects. First, FERC already has ultimate authority over the rates established by the Administrator of the Bonneville Power Administration (BPA), who is also a presidential appointee. Second, and more importantly, the issue is not so much which presidential appointees should have ultimate authority over TVA’s rates, but whether TVA customers should be entitled to challenge the justness and reasonableness of TVA’s rates. Under existing law, TVA customers do not have the ability to challenge TVA’s wholesale rates. The TVA Board is not even remotely accountable to TVA’s ratepayers, who have no recourse whatsoever in the event of an unwarranted or unreasonable rate increase. TVA customers also do not have access to information about their rates or the cost components thereof. Thus, even if distributors had a forum in which to challenge TVA’s rates, they lack the information necessary to evaluate the justness and reasonableness of the rates charged by TVA. If TVA were subject to FERC jurisdiction, however, TVA would have to file its rates publicly at FERC and would be required to provide more information about its costs.

TVA, the only utility in the United States with a AAA bond rating, also argues that FERC regulation of TVA would destroy its bond rating and harm its investors. TVA insists that its bond rating is attributable primarily to its captive customer base and its unilateral authority to establish its own rates. However, TVA’s bond rating is a function of a number of factors, including the widespread but inaccurate belief that TVA’s bonds are backed by the federal government. TVA should not be permitted to escape FERC jurisdiction (or the consumer-protection mechanisms that such jurisdiction entails) on the basis of an illogical argument that its bond rating is somehow solely attributable to its unregulated status.
**TVPPA Position**

TVPPA's most recent legislative proposal is silent as to who should have jurisdiction over TVA's wholesale sales. However, TVPPA had earlier been advocating limited FERC jurisdiction over TVA's wholesale power sales in the event of rate disputes that cannot be resolved through mandatory arbitration proceedings. As noted above, however, arbitrators lack the experience and expertise necessary to engage in the hyper-technical process of evaluating the justness and reasonableness of electric rates. In any event, FERC jurisdiction and alternative dispute resolution are not mutually exclusive concepts. Distributors who would prefer to not become involved in FERC proceedings could avoid such involvement in a number of ways. For example, such distributors could seek to include, in their TVA contracts, language providing that the distributors are required to arbitrate rate disputes with TVA prior to seeking FERC review. Parties are permitted to "contract around" their FPA rights, and FERC will generally respect parties' private contractual agreements. Under Section 4, then, distributors preferring arbitration can arbitrate any disputes with TVA in the Valley, while distributors preferring more structured, formal dispute resolution proceedings can submit their disputes to FERC.