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California Capitol Hill Bulletin

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To expand communications between Washington and California, the California Institute provides periodic faxed bulletins regarding current activity on Capitol Hill which directly impacts our state. Bulletins are published weekly during sessions of Congress, and occasionally during other periods. The e-mail edition is made possible in part by in-kind contributions from Sun Microsystems and IBM Corp.

BUSH ADMINISTRATION DENIES CALIFORNIA MTBE WAIVER PLEA

The Environmental Protection Agency (EPA), on Tuesday, June 12, denied California's request for a waiver from the two percent oxygenate requirement for gasoline. The request was made because the state is phasing out the use of MTBE, an oxygenate that has been linked to drinking water contamination. EPA's denial, in effect, will require California to use ethanol, an oxygenate made from corn. The country's largest ethanol producers had strongly opposed California's waiver request.

The State has argued that it can meet the federal clean air emission standards for clean fuel without the use of any oxygenates. In a strongly worded letter to EPA Administrator Christine Todd Whitman, California's Environmental Protection Agency Secretary, Winston Hickox, chastised Whitman for not returning his phone calls over the last three weeks, and failing to respect the state's authority. He also pointed out that "EPA's own Blue Ribbon Panel on Oxygenates in Gasoline recommended elimination of the oxygen content requirement and concluded that California's own RFG [reformulated gasoline] program would protect air quality without an oxygenate requirement."

Senator Dianne Feinstein has introduced legislation, S. 947, to grant the state authority to waive the oxygenate requirement.

FERC MAY BROADEN PRICE MITIGATION

On Monday, June 18, the Federal Energy Regulatory Commission is widely expected to significantly expand the intervention into the California electricity market which they began in April. In a Government Affairs Committee hearing this week, Sens. Joseph Lieberman and Dianne Feinstein commented that they expected FERC to broaden price controls, now active only in California and only during power emergencies, to include all states in the Western power grid and all hours of the day, and various press reports quote Administration officials corroborating the view. In a

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partial reversal, House Energy and Commerce Committee Chair Rep. Billy Tauzin (LA) and energy subcommittee chair Joe Barton (TX) wrote FERC urging such an expansion, as proposed by Rep. Doug Ose (Sacramento), chair of a House Government Reform panel with energy jursidiction.

After operating with just three commissioners for most of this year, FERC is now at its full contingent of five. Nora Mead Brownell was sworn in as the fifth Commissioner on Tuesday, following the recent addition of Commissioner Patrick Wood. Both new Bush appointees will participate in Monday's meeting and are reportedly expected to travel to California soon.

COMMITTEE TO MARK UP FEINSTEIN POWER BILL

The Senate Committee on Energy and Natural Resources, chaired by Sen. Jeff Bingaman (NM), has scheduled a hearing for Tuesday, July 19, to consider S. 764. The bill, authored by Sen. Dianne Feinstein, requires the Federal Energy Regulatory Commission (FERC) to impose cost-of-service-based rates in the Western electricity market. The Committee has also scheduled a business meeting for 9:30 a.m. on Wednesday, July 27, during which it is expected to mark up the Feinstein bill.

SENATE GOVERNMENTAL AFFAIRS ON CALIFORNIA ELECTRICITY RATES

On Wednesday, June 13, the Senate Governmental Affairs Committee held a hearing regarding "Economic Issues Associated with the Restructuring of Energy Industries," which focused primarily on the California electricity crisis.

Presiding over his first hearing as chair of the committee, Sen Joseph Lieberman (CT) noted that "California accounts for 15% of the U.S. economy. If you add its western neighbors, Oregon and Washington, which are also part of this most recent crisis, we are talking about the economic health of roughly one-fifth of the economy." He stated, "I do not believe in price controls, or price caps or other economic contrivances that inhibit the free marketplace. But we're looking at an energy market in California and the west that is not free. The fact of the matter is that the California market is not even functional. So we need to examine the appropriate role for regulators when the market doesn't work."

Senator Dianne Feinstein stated that in recent years, demand in California has increased by less than 4 percent, while conservation has reduced consumption by more than 11 percent. She announced that, on Monday, June 18, FERC may extend its April wholesale price mitigation order to the entire Western energy grid, and move it to 24 hours per day - 7 days a week (to date, the FERC price intervention has been focused only on California and applies only during a stage power emergency). Feinstein said that the question now is one of manipulation. She suggested that FERC's tying of the prices to the dirtiest and least efficient plant is an incentive to keep dirty plants and not replace them with cleaner ones. She noted that natural gas prices are three times higher in California than in any other place. Feinstein also recounted a conversation with John Bryson, CEO of Southern California Edison, who indicated that when Edison divested a generating facility that had previously been producing electricity for $30 per MWh, the company that took over began selling it for $300 per MWh. "The fact that Edison was forced to pay 10 times the price has a lot to do with the fact that the utility is now teetering close to bankruptcy." She stated that she expects her bill to be marked up on June 27.

The committee also heard testimony (which is available on the committee website) from Dr. Severin Borenstein, Professor of Business Administration and Public Policy at the Haas School of Business, University of California Berkeley (and the Energy Research Institute); Dr. William Hogan, Kennedy School of Government at Harvard University; Dr. Paul L. Joskow, Director of the Center for Energy and Environmental Policy Research at Massachusetts Institute of Technology; Dr. Alfred E. Kahn, Emeritus Professor of Political Economy at Cornell University (and the architect of airline deregulation); Dr. Lawrence Makovich, Senior Director of Cambridge Energy Research Associates; and Dr. Frank A. Wolak, Department of Economics at Stanford University.

U.C.'s Severin Borenstein said that generators base prices not on what they can afford to sell for, but on the highest price they can get in the marketplace. No one applied to build power plants from 1995 to 1998 in California, or elsewhere in the Western grid for that matter, he said, because the prospective sellers thought power prices would be too low to make a desired profit. In 1998, those prospective sellers realized they were wrong and that prices would rise, so they began building plants. But, Dr. Borenstein said, since it takes four to five years to bring a plant online, that is why we are where we are. He added that most of the demand growth over those years was not in California but in other states. He said that two things will help limit the massive transfer of wealth that is predicted for this summer. First is conservation, which has been slow to develop, particularly in the commercial sector. The second area that would help is price controls. He commented that the idea of dismissing price controls because they were poorly implemented in the 1970s is as silly as dismissing deregulation generally because of California's botched version. He concluded that, "By encouraging price-responsive demand and long-term wholesale contracts for electricity, policy makers can create electricity markets that will function much more smoothly."

Harvard's William Hogan commented that the current debate is characterized by participants "talking past one another." He said there are three options to consider: uniform price caps (which can be arbitrary), traditional cost-of-service regulation (a difficult system to implement), and bid caps (setting limits on what individual plants can bid, related to their costs, but then paying all bidders the same market clearing price). He favors bid caps, but noted that they would not help if market troubles are based on scarcity, but would repair problems caused by market manipulation.

MIT's Paul Josko commented that the recognizable problems in the California market began to emerge in summer 1998, not just last year. He said that markets operate poorly when supplies are tight, demand is inelastic, and a high proportion of power is sold on the spot market. He recommended that price mitigation be extended "24-7", loopholes be closed, other Western states be included in the mitigation program, and that California officials continue efforts to remove barriers to construction of new power plants, equalize wholesale and retail prices, and encourage conservation.

CERA's Lawrence Makovich blamed the design of the California market, rather than market manipulation. He commented that price caps can sound simple but are always more complicated to implement. When supply and demand were in balance, wholesale power costs were between $14 and $30 per MWh, which did not give an adequate, timely price signal to plant builders. He said the only way to encourage new generation is via a "periodic shortage premium." He recommended that FERC insist on California fixing a minimum number of market shortcomings before imposing price caps. He commented that price caps would not work well since half of the power is not under FERC jurisdiction.

Dr. Frank Wolak of Stanford University (and Chair of the Market Surveillance Committee of the California ISO) predicted that FERC's current plan would fail to implement the goal of market power mitigation. The current plan calls for mitigation only during emergency hours, but the majority of excess pricing to date has taken place during non-emergency hours. It also requires generators to bid power only at the "proxy bid price" for their own plants, while selling it to an out-of-state middleman would let it circumvent the rule. He noted that a megawatt in California may be sold five or ten times before it is ultimately consumed. FERC's plan creates incentives for generators to sell outside of California, as well as raise the California prices because of loopholes. He commented that, "High prices *now* do nothing to encourage investment in power. Companies look to the prices three or four years down the line when the new facility comes online."

Sen. Fred Thompson, the Ranking Republican on the Committee, expressed concern that there are uncertainties regarding the consequences of imposing price caps -- that if this turns out to be a supply-demand problem and not a market manipulation problem, the cure could be worse than the disease. Dr.

Josko noted that studies indicate that market power is not the cause of the entire problem, but represents a significant portion -- perhaps one third of the total.

On Wednesday, June 20 (at 9:30 in 342 Dirksen), the Committee will hold a hearing regarding the FERC's role associated with the restructuring of energy industries. Governor Gray Davis is scheduled to testify. For prepared testimony from Wednesday's Government Affairs witnesses, see http://www.senate.gov/~gov_affairs/061301witness_list.htm .

SENATE COMPLETES WORK ON EDUCATION BILL, CONFERENCE COMES NEXT

After seven weeks of debate and amendment, the Senate on Thursday, June 14, completed action on S.1, its bill to reauthorize myriad federal K-12 programs under the Elementary and Secondary Education Act. By a vote of 91-8, the Senate voted to substitute its language for that of H.R. 1, the companion bill which passed the House in May. A conference committee will begin work soon.

The bill includes testing provisions championed by President Bush, but does not include the President's private-school voucher plan, which would have provided up to $1,500 to help students in underperforming public schools pay for private and religious schooling. Instead, both the House and Senate bills would permit students in such schools to transfer to other public schools or obtain private tutoring. Schools would be required to publish annual report cards on their performance progress. Schools falling below standards for three consecutive years would be required to close. The Senate plan permits broadly flexible use of federal funds by seven states and 25 local educational agencies (a scheme entitled "Straight A's"), while the House version includes provisions to allow districts to use half of their federal funds flexibly without approval from the state or federal government. The Senate plan consolidates four bilingual and immigrant education programs into a single bilingual program. Both the House and Senate bills terminate a school construction program created by President Clinton, consolidate teacher hiring (class size reduction), and back President Bush's $5 billion reading proposal. A key difference is the funding level, with the Senate's higher price tag largely due to increased funding for disabled education.

During floor debate on Monday, June 11, the Senate approved by a 57-36 margin an amendment by Sen. Mary Landrieu (LA) to require that Title I funds above the 2001 appropriated levels be allocated first to Title I's "targeted grants," an authorized but to date unfunded program which directs funds to districts with high concentrations of poor children. A recent estimate indicated that California could expect to receive 14.1% of funds directed to targeted grants, a larger share than from the two existing Title I programs: the basic grant (with an 11.4% California share) and the concentration grant (with a 12.7% share). In arguing for targeted spending, Sen. Landrieu stated that the federal government spends $1,100 per poor child under Title I at a Beverly Hills school with a 10% poverty rate, and she contrasted that with the $270 spent per poor child at a Los Angeles school with a 100% poverty rate.

Also this week, the Senate turned down (22-78) an amendment by Sen Ernest Hollings (SC) which would have made the Bush testing plans voluntary, and it also rejected (47-51) an amendment authored by Sen. Christopher Dodd (CT) to specify funds for after-school programs rather than the Straight A's plan. Some Democratic Senators elected not to push for directed spending on school construction at this point, but press reports indicated that they may attempt to make such earmarks at the appropriations level.

FEINSTEIN-ENSIGN-REID AMENDMENT ADDRESSES HOLD HARMLESS

An amendment to the Elementary and Secondary Education Act reauthorization bill by Sens. Feinstein, John Ensign (NV) and Harry Reid (NV) addresses the longstanding 100% hold harmless problem on Title I funds, which has shortchanged California and other states with rapidly rising numbers of poor children but not states with relatively slower growth. The amendment codifies the compromise reached during negotiations over the FY2001 Labor-HHS-Education Appropriations Bill last fall. It provides that states will either receive either 100% of its FY 2001 funding level for Title I (a 100% hold harmless amount) or the funding level to which the state is entitled under the statute (which helps California and other growth states), whichever is greater. Senator Feinstein estimated that the shift could bring an extra $98 million to California if Title I funding is raised to the level proposed in President Bush's April budget request.

The amendment also stipulates that no hold harmless provision should be imposed on other education programs which are outside of Title I but which rely on Title I allocation data. It would also change the current updating of child poverty data, conducted by the Census Bureau and approved by the Secretaries of Education and Commerce, from every two years to every year.

HOUSE APPROPRIATIONS PASSES SUPPLEMENTAL SPENDING BILL WITH TITLE I AND LIHEAP FUNDS; PRICE CAP AMENDMENTS REJECTED

On Thursday, June 14, The House Appropriations Committee passed a supplemental appropriations bill for FY 2001. Of the $6.5 billion in total funding, $5.5 billion will be allocated to the Pentagon for various defense needs, including operations and maintenance, $734 million to cover the costs of increased fuel and energy prices, and $45 million included by Rep. Jerry Lewis (Redlands) to implement DOD's energy conservation plan in California and the Western United States in an effort to make military installations capable of serving all of their own energy needs.

In addition to Midwestern flood relief, the non-defense provisions in the bill include $300 million in additional energy relief funding under the Low Income Heating and Energy Assistance Program (LIHEAP), a boost similar to that previously added to a now defunct Energy and Commerce bill by Rep. Mary Bono (Palm Springs). Also included are $1.5 million for planning and environmental studies to boost capacity for the Path 15 power transmission line in central California.

The supplemental includes the $161 million for the Title I necessary to implement last year's conference agreement on Title I allocations to states and local education agencies. Led by Rep. Randy "Duke" Cunningham, the California Congressional delegation specifically requested these supplemental funds to ensure California's schools receive funds to mitigate the negative impact of 100% hold harmless which is perennially imposed on Title I funds. *See, Bulletin, Vol. 8, No. 18 (5/25/2001)*.

The Committee rejected 27-34 an amendment by Rep. Nancy Pelosi (San Francisco) which would have imposed price caps in the Western electricity market for 20 months. Also rejected were an amendment to provide federal loans and guarantees to improve electricity transmission and another to upgrade and repair hydroelectric dams. A fourth defeated amendment would have increased the LIHEAP boost to $600 million in fiscal 2001 and $1.4 billion in 2002.

The supplemental is expected to reach the House floor on Wednesday, June 20.

HOUSE REPUBLICANS INTRODUCE TRADE PROMOTION BILL

House Republicans, led by Ways and Means Committee Chair Bill Thomas (Bakersfield) and Subcommittee Chairman Phillip Crane (IL) introduced legislation on Wednesday, June 13, to give the President fast-track authority when negotiating trade agreements with other countries. The authority, termed "trade promotion authority" by the Administration, limits Congress to an up or down vote on trade agreements and restricts congressional review to 90 days.

The bill, H.R. 2149, does not contain provisions requiring labor and environmental standards to be negotiated as part of trade agreements. Many Democrats are expected to oppose the bill without such provisions. A markup on the bill in either the full Committee or the Trade Subcommittee may be scheduled for as early as next week. The bill was co-sponsored by numerous California Republicans, including Rep. David Dreier (Covina).

HOUSE INTERNATIONAL RELATIONS HOLDS EAA HEARING

The House International Relations Committee held a second day of hearings on reauthorizing the Export Administration Act, which expired in 1994. *See, Bulletin, Vol. 8, No. 17 (5/25/01)*. The Committee heard from several witnesses, including: Senators Phil Gramm (TX), Ranking Member of the Senate Banking Committee, Senator Fred Thompson (TN), and Rep. Chris Cox (Newport Beach).

Senator Gramm outlined his bill, S. 149, which is awaiting Senate floor action. *See, Bulletin, Vol. 8, No. 10 (3/22/01)*. He pointed out that the Banking Committee tried to strike the proper balance between encouraging foreign trade and protecting national security. The bill includes provisions that allow products that are mass-produced and widely available in foreign markets to be exported without a license. However, the President retains the unilateral right to prevent their export if he finds that national security would be threatened by it. Also, the Senate bill gives the Department of Defense the right to veto initial approval of a license application and require a more detailed investigation before a licensing decision is made. Gramm commended the Committee for closely examining the issues surrounding reauthorization and encouraged it to follow the approach taken in his bill.

Senator Thompson, however, expressed concerns with S. 149, and its relaxation of controls on high performance computers. Although he testified that he is not wedded to the use of MTOPs as the appropriate measure of performance, he felt strongly that some control on computer exports was required for national security purposes. He also argued that the prerogatives given to the President in S. 149 would be too complicated to administer and thus ineffective.

Rep. Cox urged the Committee to raise the penalties for export violations as a significant step in enhancing national security. He also stated that unilateral controls on exports were inadequate and the United States must pursue a multilateral control regime with its trading partners. Cox also called for an effective post-shipment verification process and appropriate checks and balances on the U.S. agencies with jurisdiction over export control decisions.

Testimony of these and other witnesses can be obtained through the Committee's website at: http://www.house.gov/international_relations .

HOUSE PASSES PACIFIC SALMON RECOVERY ACT

The House on Wednesday, June 13, passed the Pacific Salmon Recovery Act (H.R. 1157) by a vote of 418-6. The bill authorizes $200 million annually for three years to California, Alaska, Idaho, Oregon and Washington for local salmon conservation and restoration programs. In addition, Indian tribes in those states would also be eligible to receive 15 percent of the funds. The funds will be matched by state governments.

The House passed similar legislation last year, but the Senate did not take up the bill.

GOVERNOR ANNOUNCES $54.8 MILLION IN CALFED GRANTS AND LOANS

On Monday, June 4, Governor Gray Davis announced $54.8 million in projects approved by the CALFED Bay-Delta Program to improve California's water resources and management. The projects are the latest in a series of state funding for the Program that total more than $500 million this year. *See, Bulletin, Vol. 8, No. 18 (6/8/01)*.

The projects, funded by the Department of Water Resources through the 2000 Water Bond (Proposition 13) and other state funds, include pilot groundwater storage projects, installation of ultra-low flush toilets, local watershed planning and assessment projects throughout the state.

For more information on the projects or CALFED log onto: http://calfed.ca.gov .

PPIC Examines Impact of Minority Districts on Voter Participation

On Wednesday, June 13, the Public Policy Institute of California released a study entitled *The Effect of Minority Districts and Minority Representation on Political Participation in California*. The study provides empirical evidence in the debate over whether creating majority-minority districts leads to greater participation by minority groups in the political process. Researchers using voting statistics from the November 1994 congressional elections and census data compared turnout rates in the state's 13 majority-minority districts with those in majority-white districts.

In general the study found that Latino and African-American voter participation is highest in congressional districts where they are able to play a prominent role in deciding political outcomes. Latino registered voter turnout was 33% higher in California's six majority Latino congressional districts compared to Latino turnout in majority white districts. In districts where Latinos and African-Americans were more evenly matched and together make up the majority, Latino turnout was 30% higher and African-American turnout was 7% higher than in majority-white districts.

The report presents an in-depth analysis of findings as well as policy implications. To view the report in its entirety, visit the PPIC website at http://www.ppic.org .

California Institute Hosts Breakfast with Rep. Adam Schiff

On Tuesday, June 12, the California Institute sponsored a breakfast for supporters with a Rep. Adam Schiff to discuss bipartisan issues and their impact on California. Pfizer generously hosted Tuesday's breakfast. Rep. Schiff discussed his role in starting Freshman for Finance Reform, a bi-partisan effort which supports the McCain-Feingold Campaign reform legislation. He also discussed a bill he introduced which seeks to expand Head Start funding and strengthen the program by developing a national enrollment campaign and a reading readiness component.

Rep. Schiff discussed plans to introduce other education-related legislation, specifically in the area of higher education to expand the Hope Scholarship and Pell Grant programs, as well as science research funding. Schiff also discussed the issue of water quality and fielded questions regarding trade and energy, as well as school to career, Hope scholarships, Pell Grants, and other education issues.

Letter Circulating in Support of DOE Office of Science

Reps. Ellen Tauscher (Pleasanton) and Judy Biggert (IL) are circulating Dear Colleague letter directed to the House leadership and appropriators in support of the Department of Energy's Office of Science. The letter urges appropriators to increase fiscal year 2002 funding for the Office of Science above the level appropriated in FY 2001. According to the letter, the Office of Science is the nation's primary supporter of the physical sciences and increased funding will allow for the fullest utilization of scientific talent and the best research facilities.

California received $653,910 in funding through the Office of Science in FY 2001, approximately 23% of the overall funding. A similar letter was circulated last year and received bi-partisan support with over 90 members signing it, including about a broad cross-section of Californians of both parties. For more information on the letter, or to cosign, contact Paul Doucette at x53515.

Global Entertainment Outlook Predicts Strong Growth

A five year global entertainment outlook predicts the entertainment industry will grow past $1 trillion annually and reach $1.2 trillion by 2005. According to the recently released Pricewaterhouse Coopers report, *Global Entertainment and Media Outlook: 2001-2005*, this growth will be due to an explosion in the Latin Market and entertainment viewed over broadband Internet systems. The report examines the growth in the entertainment industry in the following areas: Filmed Entertainment; Television Content; TV Distribution; Recorded Music; Internet Advertising and Access Spending;

Magazine Publishing; Newspaper Publishing; Book Publishing, Radio and Out-of-home Advertising; Theme Parks and Amusement Parks; and Sports.

According to the report, filmed entertainment, one of California's leading industries, will experience an increase in spending, with a 6.6% compound annual growth rate increasing from $68 billion in 2000 to $93 billion in 2005. Similarly, the televison content-broadcast and cable network market will grow at a 9.4% compound annual rate, increasing from $107 billion in 2000 to $168 billion in 2005. According to the report, another area of the industry, Internet advertising and access, will drive the U.S. market with a 14% compound annual growth rate by 2005. It is predicted to be the fastest growing segment globally over the next five years.

117,000 H-1B VISAS GRANTED BY INS

To date this year, the Immigration and Naturalization Service has issued 117,000 visas for skilled workers to be employed by U.S. companies. That number does not include foreign workers exempted from the cap, which probably makes the total number of visas higher. Last year by this time, the cap of 115,000 visas had been reached. INS also estimates that it has about 40,000 applications still pending. Congress expanded the program last year to allow up to 195,000 H-1B visas annually, and excluded from the cap employees of universities and other research institutions.

In related news, INS has instituted a new H-1B processing program. Under the program, employers who pay an additional fee can have their petitions expedited. The additional fee is $1,000, on top of the standard $1,000 that is paid by everyone. INS guarantees that the expedited applications will be processed within 15 days, when the added fee is paid.