

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

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In the Matter of: :

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SOUTHWESTERN TECHNICAL CONFERENCE :

:

ARIZONA PUBLIC SERVICE COMPANY : Docket No.

EL PASO ELECTRIC COMPANY : RT02-1-000

PUBLIC SERVICE COMPANY OF NEW MEXICO :

TUCSON ELECTRIC POWER COMPANY :

:

WESTCONNECT RTO, LLC : Docket No.

: EL02-9-000

:

REMEDYING UNDUE DISCRIMINATION : Docket No.

THROUGH OPEN ACCESS TRANSMISSION SERVICE : RM01-12-000

AND STANDARD ELECTRICITY MARKET DESIGN :

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Wednesday,

September 24, 2003

Pointe Hilton at Squaw Peak

Apache Ballroom

7677 N. 16th Street

Phoenix, Arizona

The above-entitled matter came on for hearing,
pursuant to notice, at 10:12 a.m.

BEFORE:

MODERATOR:

PAT WOOD III, Chairman

Federal Energy Regulatory Commission

APPEARANCES:

PAT WOOD III, Chairman, Federal Energy Regulatory
Commission

NORA BROWNELL, Commissioner, Federal Energy
Regulatory Commission

WILLIAM MASSEY, Commissioner, Federal Energy
Regulatory Commission

MARC SPITZER, Chairman, Arizona Corporation
Commission

LYNDA M. LOVEJOY, Chairwoman, New Mexico Public
Regulation Commission

CHARLES REINHOLD, WestConnect Project Manager

DAVID WIGGS, General Manager, Los Angeles
Department of Water and Power

Panel - Transmission Owners

STEVE GLASER, Senior Vice President, Tucson
Electric Power Company

STEVE WHEELER, Senior Vice President, Regulation,
System Planning & Operations, Arizona Public
Service Company

DAVID AREGHINI, Associate General Manager, Power,
Construction and Engineering Services, Salt River
Project

STEVE FAUSETT, Senior Vice President,
Transmission, Tri-State Generation and
Transmission

TOM JONES, Grand Canyon State Electric
Cooperative Association

RONALD MOULTON, Manager, Electric Power
Restructuring, Western Area Power Administration,
Desert Southwest Regional Office

Panel - Other Stakeholders

MICHAEL M. GRANT, Gallagher & Kennedy

STEVE HUHMAN, Director, Market Design &
Regulatory Affairs, West Region, Mirant Inc.

JOHN WOODLEY, Morgan Stanley Capital Group, Inc.

DENNIS L. DELANEY, K.R. Saline & Associates, PLC,
for Arizona Consumer Owned Electric Systems

SCOTT GUTTING, Energy Strategies, Inc.

CHRIS ELLISON, American Wind Energy Association

STEVEN C. BEGAY, General Manager, Dine Power

Authority

STEPHEN AHEARN, Director, Arizona's Residential Utility
Consumer Office (RUCO)

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P R O C E E D I N G S

OPENING REMARKS OF PAT WOOD III, CHAIRMAN, FEDERAL
ENERGY REGULATORY COMMISSION

CHAIRMAN WOOD: Good morning, I'm Pat Wood, Chairman of the Federal Energy Regulatory Commission. And since we have a voting quorum here I'll call this posted open meeting of our Commission to order and want to thank you all for coming.

This is the seventh, I believe, the sixth or the seventh of our regional working conferences on the regional transmission organizations for the electric power industry across the country. In the summer of last year our Commission put out a proposed rulemaking called the Standard Market Design Rule to talk about where we go as a nation in a region by region basis with the developments in the wholesale power industry.

As a follow-up to the California issues of 2000 - 2001 and to the changes in the industry brought about by the rapid exit of Enron and others we thought it was important to provide some structure and some guidance from our perspective as the federal regulator of the interstate power grid in the wholesale power markets to try to shape some positive development so that customers will get benefits as opposed to getting shellacked by the wholesale power market.

So in response to a lot of comments we got from

both state commissions and AGs and market participants, utilities, competitors, customers and others the Commission in April of this year put out a White Paper which is a announcement of our revised approach toward standard market design and toward RTOs that's really framing our discussions here today. As part of that reorientation of our direction we committed to each other and to the industry to go out to each region and really do an assessment of where wholesale power market development is at this time.

And so that's our goal here today. I appreciate the hard work that a lot of folks at the state commissions' staff, the state commissioners and our own staff and market participants put together to do a nice balanced agenda today.

And a couple of things I just want to say as far as kind of overview comments here. I want to kind of reemphasize one of the key points of that White Paper that we put out in April which is the desire to really customize market development on a region by region basis. This is called regional deference or flexibility but, quite frankly, it's what we call common sense too.

As a practical matter the development of power markets in the country are at very different phases depending on where you are. We had the first of these conferences in Boston where recent developments in their

market have led to a pretty advanced state of competitive markets.

We followed that with a conference in Atlanta where in the deep south they have a much more rudimentary or basically initial approach toward competitive markets. And so there is a lot of diversity in the country just with the seven stops that we've made on this tour. And I expect that the Southwest will be no different.

But we want it, we mean what we say when we talk about deference to regional desires for how their market ought to be fashioned. Hope we'll hear a good part of that today.

I do want to add that at the end of the day we do have kind of an open discussion, I wouldn't call it open mike because it's not quite like a comedy club we hope, but it is an open discussion to make sure that open ideas or other perspectives do get into the public record here. And we are, as you know, taking this and making this available as a public part of our record for this docket.

We hear a lot as we go around the country about the importance of protecting something called native load. And as an illustrious predecessor of mine on FERC said, everybody is somebody's native load. So as a practical matter we do want to make sure customers are protected. But we also want to understand and explore what that means here

in this region. This was an issue in the WestConnect filings that our Commission has approved over the last two years that we've been working with WestConnect.

And I should add as a prior job I was a state commissioner in Texas and we worked, I don't know, Jess, how long ago was it? with DesertSTAR, I guess '96 or 7. So we've been talking about this for a long time, folks. And I kind of think what we're interested today is to try to give the effort to see how can we actually start walking it as oppose to talking it. And I am looking forward to hearing some comments on that.

In our White Paper in April we laid out eight issues of the power market which will be I know Charlie's going to mention those when we talk about the WestConnect developments in a moment, but one of the things we indicated there was rather than a big bang approach that we had envisioned in our original rule that a sequenced, phased-in approach of market design issues should be, would be entertained and would be welcome and that actually would probably make sense if we approached it that way. And we've seen that to be pretty well received in other regions of the country that don't quite want to go to the fully developed New England TJM style market yet but want to get some of the early low-hanging fruit, low cost, high benefit achievements done.

And one of the things that I do want to explore here today because I have seen the layout of some of the presentations here is at what stage do we actually get an independent entity involved here in looking at the power grid in the Southwest? In all the other regions of the country that has been a predicate. In fact, everybody has accepted that in fact what you need to have here is an independent, by independent we mean independent of market participants, the person administering the power grid on behalf of everybody has in fact not got a generation interest or load serving entity interest involved.

And this is actually the first place where I have seen some indication that that would be not at the front end but at the back end of a process. And I've got an open mind but I want to kind of make sure that we do delve into that issue here.

A lot of these kind of basic issues for setting up a wholesale power market do have low costs. And I want to understand those. I think as we've seen around the country there are concerns about moving to a day-ahead market to more probably accurate but more complicated congestion management systems where you have congestion that needs to be dealt with on a system. But there are a lot of other aspects of setting up a wholesale power market such as getting an independent grid operator or regional planning

process, a tariff that is applicable and open to all customers who are willing to pay the bill, simplified tariffs, understanding of how rates work both at the wholesale and the retail level.

Some of those things aren't really costs. They don't have cost to them, they just have to be done. And I think I want to understand here what we have to do both on the political level and on the business and customer level to overcome, to get to those what I call low cost, high benefit structures for the electric power industry.

I do want to say that we can work together to benefit the customers here in the Southwest. There are a lot of opportunities I think. I grew up one state over from the Southwest but I think I come from the same kind of culture here that kind of thinks well, if it ain't broke don't fix it, which is kind of issue number one or, number two, what do the feds know?

Well, when there's states that don't agree that's where feds come in. And, you know, these issues do spill outside the boundaries of one state. I think from our own perspective as folks who come from different backgrounds my colleagues and I, you know, understand that somebody has got to make the calls. But we'd much prefer that to be dealt with in a region-centered local solution-driven problems than at FERC. We're to be the catalyst. That's our job.

We want to be a catalyst for getting a beneficial wholesale power market set up.

I could go on for days about where I think the benefits are because, quite frankly, there are quite a few. We saw in our transition in the gas industry that our Commission was in charge of in the '86 to '92 time frame just how much significant benefits there were for customers in restructuring the gas industry. We may not see those as much today as gas has doubled in price but, quite frankly, the competitive market over the last 15 years in that industry has bought significant savings to customers. Some quantify it at \$600 billion that has stayed in customers' pockets from just that much smaller industry going through a more radical restructuring than what we're talking about here on the electric side.

So I think there are a lot of customer benefits. But there's also the investor certainty and the technological issues that we've seen in every other industry that comes through the competition track that I think we could certainly look at here.

We do understand the need for market monitoring. We certainly know this is our first step here in the West. We've got another one set for California in November and an unscheduled one for the other market here in the northwest. But this particular region of the country suffered a lot

from relatively unmonitored, unstructured markets or differently structured markets back in 2000 when Commissioner Massey was here and before Nora and I came on board. And we certainly have been dealing with those issues really for the balance of our time on the Commission. Nora and I have now passed our two year anniversary on the Commission together.

But the issues in the West really cry out for a need to have a transparent monitorable market so that customers do not go through the same kind of dislocation and pain that they went through two years ago and which continues in some regard today. So I know there are a few issues to be discussed on that.

The coordination of new generation in the Southwest with the regional transmission planning, just had a visit with some folks from here in Arizona at breakfast over some of the expansion of transmission line issues that I know are very present here in this particular state that kind of distinguish it perhaps from other parts of the West. But those issues of regional planning we do want to endorse and support the SSG-WI process that has been very successful I think so far in at least framing up the issues for people to discuss. I think the discussion probably needs to translate now into some action. But I do think that the groundwork through the industry-led working sessions and discussion

groups has been productive.

I know some people have lampooned it as being professional discussion societies. There is an article in some periodical that all the regulators get. And we read those. But I do think that we do owe it to all the people who have done a lot of hard work both that are in this room today, and I see some of your faces nodding as you know what I'm talking about, but across the whole west to really try to get in response to the '96 outages a lot of significant changes were made on a regional basis that were accelerated after the 2000 crisis. But I think we do owe it to all of our customers out here to learn from all those things and then do something about it.

So we want to again be supportive of that effort and be as constructive partners here from the FERC side as we can possibly be on that.

There are a lot of other issues that we could talk about. And I think by the end of the day they'll be all put out on the table. So without a lot of further ado again I want to thank our friends at the state commissions here from Arizona and New Mexico. I know we've got staffers from Texas and I believe Utah. Am I missing anybody? And Nevada as well here. And thank you all for coming as well. And all the folks and the different participants in the marketplace, and you're what it's all about, so serving your

customers is what we want to do right.

I would like to ask my colleagues Nora and Bill for any thoughts they might have.

STATEMENT OF COMMISSIONER NORA BROWNELL, FEDERAL ENERGY
REGULATION COMMISSION

COMMISSIONER BROWNELL: I am anxious to get on with the day but wanted to say thank you for all of you who hosted me in the last week. I had a wonderful tour with our colleagues in the Southwest. And recognize that we have a long way to go to developing stronger working relationships, spending time here and later in the day we'll introduce our western team. But I learned a lot and I'm anxious to come back.

And I appreciate the thoughtfulness with which people approached the issues that were frankly not limited to their state, not limited to narrow sectors of their state but really looking out for their native load as well as the market participants in the region as well.

And I'm also grateful to the people from SRP, the coops, the companies themselves who really identified in a far more meaningful way some of the business challenges and priorities that they're trying to incorporate into the discussion of creating an RTO here.

So I had a wonderful time and I hope I behaved myself so I can come back.

STATEMENT OF COMMISSIONER BILL MASSEY, FEDERAL ENERGY
REGULATORY COMMISSION

COMMISSIONER MASSEY: Well, I wanted to offer my personal thank you to all of you who have taken the time to show up at this important session this morning. I chaired my first regional conference here in Phoenix on the issue of forming an RTO in 1998 when the issue was whether to form DesertSTAR. So there have been good discussions, fruitful discussions going on in the Southwest for years about this very topic. And we will continue those discussions today.

I'm here not to talk but to hear your views about how we can continue to move forward and get the rules right in wholesale markets in the Southwest so that we can get on with the customer benefits that we think will flow from that.

So thank you for attending and I look forward to your frank comments.

CHAIRMAN WOOD: At this time we would like to turn it over to our host commission chairman from both the Arizona Commission, our friend Marc Spitzer, and Lynda Lovejoy from the New Mexico Commission whose utilities are the primary anchors of the WestConnect RTO. It does spill over into other states. But we appreciate your kind invitation and your leadership on trying to really bridge some of the federal and state issue that have come up over

the last year as we've gotten closer to talking about the details here.

And we certainly welcome and appreciate, Marc, your leadership and your invitation because I know, as you told me a moment ago, is your legislative district from the old days. So we're glad to be in your home. Turn it over to you.

STATEMENT OF MARC SPITZER, CHAIRMAN, ARIZONA CORPORATION COMMISSION

MR. SPITZER: Thank you. Mr. Chairman, Commissioners, thank you very much.

I'm Marc Spitzer. And I'd like to first welcome you all to the sunny state of Arizona. For those just in some confusion, the picture in the paper this morning was not of me.

(Laughter.)

So I remain a commissioner. And I would like to take this moment to introduce two of my colleagues, Commissioner Jeff Hatch-Miller and Commissioner Mike Gleason. And also Commissioner David King from New Mexico. And after myself and Commissioner Chairman Lovejoy speak we'd be happy to invite our colleague commissioners to make comments.

Just as the Chairman noted that there was a quorum present and this item was noticed by the FERC, similarly,

the Arizona Commission has a quorum present and we noticed a notice of joint appearance. And consistent with that notice I want to mention that the comments I'm about to make are in my personal capacity and not the statements or comments attributable to the Commission. And certainly our colleagues are invited to make comments as well.

There are five points that I want to make as introductory remarks to this conference this morning. The first is a doctrine that I use when I teach government, politics, and that is healthy tension. I refer to this often in our unique federal system as well as discussions among branches of state government, legislative, in which I served four terms in the state senate, the executive branch and the judicial branch.

And the term "healthy tension" came from the Federalist Papers. And the discussions and the very difficult, occasionally contentious issues raised by the Chairman I think reflect that healthy tension in the best sense of the word. There is this healthy tension between the federal and state governments as well as among branches of government. And that is the purpose of this conference I think this morning to resolve that in a productive, positive manner. And I am appreciative of the FERC being here.

It is when the tension becomes unhealthy that it is counterproductive to our mutual constituents. And

unfortunately we've seen some examples in the recent past, particularly with respect to California, that in all candor I must say generated an unhealthy tension. Certainly it is appropriate for state governments to assert their legitimate interests. Some folks in our staff are back in Washington today on a matter of importance to the state of Arizona with regard to natural gas. And that's appropriate and that is consistent with this, again, concept of healthy tension envisioned by our founding fathers.

But the gratuitous attacks on the FERC in connection with the California situation which in large measure were events not attributable to any federal policy but instead to the state policies are not only inappropriate but counterproductive again to the citizens. And this conference I am extremely confident given the long history of blunt talks but very civil talks from folks in this part of the country that we will maintain this concept of civility and that the discussions will be in the model of this healthy dialogue as oppose to one that is acrimonious. And the dialogue will be based on an effort to solve problems rather than to apportion blame or find scapegoats.

The second point I want to mention I caption "Wall Street" in my little comments. At a recent conference I was told by a chairman of a state commission that the Wall Street model for the electric utility industry is a

vertically integrated monopoly cost-of-service regulation. And that's the only model that Wall Street will now permit. And I would point out to those in the audience that Wall Street loved Enron in 1999 at \$90 a share.

So I venture to say that the pendulum swings one way and the pendulum swings the other way. And I think those in this room understand that there are many models for successful governance. I'm not excluding by any means the potential for a state commission to make a determination that the vertically integrated cost-of-service monopoly model is an appropriate model but there is room for a merchant model. There is room, as is known widely in the western United States, for public power, for various financial and economic governance models. And I think our system works best where these models are free to compete in a free market.

And ultimately I think the pendulum will reverse but I think I do need to take a moment to at least address that issue that has been raised. And in my judgment what has been proposed in the White Paper is a means for these various models to compete based on quality of service, price and other considerations to the benefit of the ratepayers because that's what this endeavor is ultimately all about, regardless of whether we sit in the federal government, the state government, public sector, private sector, ultimately

the best interests of the ratepayers in my view is served by a model that does provide for multiple business models. And to me that is one of the commendable aspects of the White Paper.

The third point I've labeled "Adam Smith." Adam Smith wrote "Wealth of Nations" in 1776 and among the economic models that were refuted in his ode to capitalism was a doctrine called autarky. Autarky posits that there should be no trade. And Adam Smith debunked that fairly vigorously. And you haven't seen autarky reappear as an economic model since 1776 with one exception, and that was Adolf Hitler's Nazi Germany. And that I think we would all agree is a failed model.

There must be trade, there must be free trade. And ultimately we have to come to grips with the threshold question of whether electricity is a commodity. Now I've reached the determination that it is a commodity. It should be subject to trade. The trade needs to be free. The trade needs to be fair. There are certainly aspects of the trade that need to be regulated and adjudicated and the details of that regulation and adjudication are a subject of the remainder of this conference. But the predicate assumption is that free trade is a good thing.

In the short run you have some degree of cost shifting. Just as Washington State ships apples to Arizona

and Arizona ships citrus to the state of Washington, in the long run everyone benefits from free and fair trade. And when I use the word "fair" some people forget that Adam Smith was also a theologian and he discussed in his concept of economic governance and his concept of a properly functioning capital system the concept of virtue which some entities disregarded rather blatantly in the recent past. But virtue is consistent and part of our capital system and to the degree that entities doing business ignore virtue I think that's where regulators step in.

My fourth point is during my tenure in the state legislature I always liked to say "yes but" rather than "hell no." It's more pleasing to those in a discourse and, again, I think it's more productive to the people that we represent. And the reception that I've observed from the various business entities within the state of Arizona some of those producers, some of those users of electricity, large commercial, public power, industrial utilities is a response to the White Paper of "yes but" as opposed to "hell no." And I think that's productive and I look forward to that type of discussion ensuing during the remainder of the conference.

And then finally I would like to express appreciation, appreciation to the fact that all three FERC commissioners are present this morning here in Arizona,

appreciation for putting on not only this conference but we had a very productive conference on gas storage last month, and all of the efforts of the FERC to work with and cooperate with not only our commission but the entities that do business in Arizona to the ultimate benefit of the ratepayers. I'd like to express my appreciation to Chairman Lovejoy and Commissioner King for their presence this morning as well as to all those in the audience that are attending in the hopes of improving the circumstances in which they do business to the ultimate benefit of all the ratepayers of not only the state of Arizona but of the Southwestern United States.

So, again, thank you. I very much look forward to this conference and the full and fair uninhibited discussion of these important issues.

Mr. Chairman, thank you very much.

CHAIRMAN WOOD: Thank you, Marc.

STATEMENT OF LYNDIA M. LOVEJOY, CHAIRWOMAN, NEW MEXICO
PUBLIC REGULATION COMMISSION

MS. LOVEJOY: Good morning everyone, Chairman Wood, Commissioner Brownell and Commissioner Massey and all of the dignitaries sitting up here.

Mr. Chairman, if you could just indulge me for a moment I'm going to do something I should have done last week. It's my tribal tradition that when you invite a very

special guest to your home and in this case to the state of New Mexico you honor them with a small token of appreciation. And last Wednesday I did not do that. I broke tradition. My elders are very annoyed with me. And so today I'm going to correct the wrong that I did last week.

So I'm going to present Commissioner Brownell with a small token of our appreciation for coming to New Mexico. And I did invite her so it's my responsibility to present her.

I'm glad to get rid of this box.

(Laughter.)

MS. LOVEJOY: Thank you very much.

COMMISSIONER BROWNELL: I was honored to visit.

MS. LOVEJOY: Thank you.

And here, you can have the box.

(Laughter.)

COMMISSIONER BROWNELL: Thank you.

MS. LOVEJOY: You're very welcome.

I would like to just make a few remarks. My statement today is in concert with the Commission views previously expressed to our New Mexico congressional delegation through letters dated July 24, 2003, June 11 and December 24, 2002.

We have five commissioners, each elected by

district. I represent the northwest quadrant of New Mexico, the state's most important reason for energy and electricity production. It is the source of most of the coal and natural gas that fuels the power plants located in the Four Corners area.

As the fifth largest state, with fewer than two million people, New Mexico has a very low population density statewide. By far the highest concentration of energy users is found along the Rio Grande Valley, including Santa Fe, Albuquerque and Las Cruces. In terms of average revenue per kilowatt hour for combined customer classes New Mexico ranks fourth highest in the region and is below both the regional and national averages.

New Mexico legislature, like many others, was originally attracted by the concept of retail competition. And in 1999 passed the New Mexico Electric Utility Industry Restructuring Act. As it became apparent that retail competition was not likely to bring benefit to New Mexico customers the legislature took a second look at restructuring and delayed full implementation until 2007.

In January of this year, recognizing the failure of the California energy market and its effects on the economies of several western states, including Montana and Washington, New Mexico legislature completely rejected electric retail competition. However, the legislature did

allow New Mexico's electric utilities to move to a holding company structure with more than one operating company.

The PRC's legislative mandate is to act in the public interest. The PRC's basic job is to regulate those utilities so that reasonable and proper services are available at fair, just and reasonable rates. Regulation by the PRC should result in the attraction of capital investment to provide for the development of needed plants and facilities.

New Mexico is a major energy producer and exporter with abundant natural resources in the form of coal, natural gas, uranium, solar radiation and wind. Although two natural gas fired merchant plants have been canceled or postponed in New Mexico in 2002 due to market uncertainty, the country's third largest wind power facility located at House, New Mexico, is scheduled to come online next Wednesday on October 1.

In addition, proponents of the Dine Power Authority are trying to develop a very large transmission line on lands held by the Navajo Nation. Because of New Mexico's prominence as an energy producer in the Southwest, it's people must balance significant air quality and land use issues related to energy production and transport with the economic benefit of those activities. Given that there is no retail competition in New Mexico, the PRC must take great

care to ensure that New Mexico customers do not lose out to energy users out of state.

I'm very concerned that the best recent studies point towards this trend. FERC's own economic assessment of RTO policy released in 2002 predicted net power flows that are likely to pose substantial shifts in how power is generated, marketed and priced within New Mexico and surrounding areas. Other studies contain transmission infrastructure expansion and power pricing forecasts that suggest likely increases in retail rates in New Mexico consumers.

As a result of FERC's proposed transmission policies it's no secret that California as a net energy importer will continue to rely on excess power produced in other western states. The DOE report predicted that implementation of SMD would cost New Mexico and Arizona consumers more than it will benefit them. In addition, the report done for the PRC and the New Mexico legislature at the end of 2002 predicted an increase in the peak demand in the Southwestern region that would reduce the capacity margin.

I'm concerned that to date no study has predicted positive benefits for New Mexico native load customers. I believe that any RTO proposal involving New Mexico utilities should show the benefits outweigh the costs and risks. The

western wholesale power market has grown up based on a voluntary approach and is self regulated. In our view it has functioned very well so far.

Our Commission to date has supported the idea of voluntary RTOs. Because the various regions of the country differ in the circumstances in which their electric utilities operate what works in one region may not be good for another. A voluntary RTO processes would help in the development of region-specific solutions.

Would FERC consider the idea of implementing RTOs first in the eastern regions of the country without setting a precedent for other states where very strong support for leaving the western states time to study and develop regional alternatives that works best for them. We support and approach this entire setup transmission issues that is based on full engagement and dialogue involving FERC and all of the states in the Western Region.

Our Commission has supported the concept of RTO formation on a voluntary basis but we need to see if the benefits outweigh the costs, provide us with an opportunity for full engagement.

Thank you, Mr. Chairman, for the opportunity to address you from New Mexico.

MR. SPITZER: And, Mr. Chairman, if I may, I would certainly like now to invite our fellow commissioners to

make some comments. Commissioner King?

STATEMENT OF DAVID KING, VICE CHAIRMAN, NEW MEXICO
PUBLIC REGULATION COMMISSION

MR. KING: Mr. Chairman, we do appreciate you coming to Southwest Arizona. We very much appreciate your comments in looking at each region and trying to distinguish each of those regions.

As a vice chairman I am listening to Marc Spitzer's comments and I want to thank him for his help in New Mexico during the legislative session helping us get some major legislation passed. And so he said he's been more effective in New Mexico than in Arizona but he's very helpful to us out there.

And so, Mr. Chairman Spitzer, we appreciate that.

MR. SPITZER: Thank you.

MR. KING: I'm glad to be here with our distinguished Chairwoman Commissioner Lovejoy. And as the vice chairman I think one of the points that Chairman Spitzer mentioned is a healthy tension. We've been debating the RTO issue and have taken stands to the congressional delegation.

And I'd like to read a letter today that Commissioner Block, who is the longest running commissioner we have in New Mexico, signed with me. And I think that Chairman or Commissioner Baca who is in Chile doing some

NARUC business and not with us today, her assistant Judy Kelso is here, supports this position. So it's a majority position and wanting to go forward in the RTO a little more aggressively.

And this is to Senator Domenici as Chairman of the Energy Committee and also to the House Energy and Commerce Committee re the regional transmission organizations.

We state: "As state utility regulators from the Western Region of the United States we write to you to express both our support for continued development of regional transmission organizations and our concern regarding potential amendments to the pending energy legislation that may inhibit RTO development in our region and across the country.

"As has been recognized by both the media and the public in general after the August 14 blackout, a regional approach to the management of the flow of electricity across multiple states is key to ensuring reliability. Well-functioning RTOs work to provide reasonably priced and reliable electricity to consumers and businesses. This is a similar conclusion that was reached by Department of Energy task force following the 1996 western blackout.

"RTOs are key components in the creation of a well-designed and effectively functioning regional market. The recent blackout highlighted structural problems with the

grid in the affected regions. Although we have been assured by our local utilities that such problems do not exist in our states, we recognize the expansion of participation in RTOs would also help address future problems with the grid as they are discovered.

"Further, the development of voluntary RTOs would help improve responses to problems in the grid by having an effective regional traffic cop with a reliability mission to manage any future incidents. It would also help improve the climate for investment and transmission infrastructure to enhance the reliability of the grid.

"Furthermore, we believe the electricity title should neither disrupt regional markets nor stall RTO developments in the region. Development of wholesale market structure should be left up to the states and the responsible federal agency. Thus, we urge you to support efforts to establish voluntary RTOs. We believe it is imperative to move forward with efforts to bring the benefits of RTOs to customers.

"Thank you for your consideration."

Signed by myself as Vice Chairman and Commissioner Block.

There are issues we have to look at. And I know that FERC's looking at that as well. The reliability issue certainly, but we have to look at reliability beyond our

borders and state to state, as we talked about in the meetings with Commissioner Brownell in Albuquerque. While we may be very well set in one state, if something happens in our neighboring state and we're not cooperating it could endanger us there even though we think we have everything covered. That was obvious in the recent blackout.

So I think it's important to see that public power as everyone looks in this area that we look at the cost/benefit analysis, but in looking at the several months now that I've been on the Commission it looks like to me the best avenue that we have would be to use the RTO and go forward with that. We've debated and debated. We've got to have communication. We're not an island in New Mexico. Our economy, we had a major vote yesterday on our state permanent fund from oil and gas. We're fourth and fifth in oil and gas production in the country. And that means we sell a lot of oil and gas much beyond what we use. We have to have that communication. We have to have that transmission ability.

And we're eager, I know our governor has voiced that who is becoming Chairman of the Western Governor's Conference, Governor Richardson. We have Senator Domenici and Senator Bingham on the Energy Committee. And we're hopeful that we can be part of the solutions and push the RTO process and move forward in having that communication

and that working team relationship between states and the federal government.

Thank you very much.

CHAIRMAN WOOD: Thank you, Commissioner.

MR. SPITZER: Commissioner, we'd be happy to buy your oil and gas at reasonable price.

MR. KING: We'd be happy to sell it to you at a reasonable price.

MS. LOVEJOY: Mr. Chairman, may I just clarify something?

CHAIRMAN WOOD: Yes.

MS. LOVEJOY: I know this is very difficult for me to say but the letter that was just read by the vice chairman is not an official letter under our New Mexico Commission rules.

CHAIRMAN WOOD: And that's fine. We understand how different commissions operate differently.

Appreciate the sentiments though from everybody on the state side. And I think I want to reiterate from Bill and Nora's perspective and my own that we, certainly Nora and I were both state commissioners prior to taking this job, how important we view that relationship. Kind of whatever the law is quite frankly we've got to make it work because that's what we've sworn to do under our respective laws and constitutions. So we will do that.

MR. KING: Mr. Chairman, if I could respond, I know that Chairman Lovejoy knows on next Tuesday's agenda to go over this letter. Commissioner Baca is doing NARUC business as we said out of the country. She will be back next week and we will hopefully formally take that action on Tuesday.

CHAIRMAN WOOD: Okay. Thank you all very much. And I want to invite any of the other representatives from the other states. This is our panel right now for state thoughts and perspectives that might help frame the discussion and I would invite any of the other commissioners from Arizona or staff from the other states who might want to add any thoughts to frame today's debate.

(No response.)

CHAIRMAN WOOD: Okay, thank you all.

Next we're going I think why don't the five of us go sit over here somewhere and let our next two panelists move over to the front and center here so everybody in the room can see them.

While we are moving around I want to introduce Charles Reinhold who has been the project manager I think, Charlie, since I've been on the Commission, I know before then.

MR. REINHOLD: Two years now.

CHAIRMAN WOOD: Three years now?

MR. REINHOLD: Two.

CHAIRMAN WOOD: Two, for the WestConnect project. And he'll start with that. Then after then we'll have an update from David Wiggs who's an old friend of mine but a general manager now at the L.A. utility, L.A. Department of Water and Power, to discuss the WestConnect public power initiative here in the West that was the subject of a recent announcement that we all heard.

So without further ado we'll turn it over to you two guys.

STATEMENT OF CHARLES REINHOLD, WESTCONNECT PROJECT
MANAGER

MR. REINHOLD: I have to report to you that one of the FERC commissioners just mentioned up here that he doesn't know where we're going. So while we rearrange here and try to get hooked in so you all can see the presentation we'll just ponder that for a moment.

(Pause.)

(Slide.)

MR. REINHOLD: With this handheld mike I think this may work a little better. For presentation purposes it may be a little tricky here working both the machine and trying to read from some notes.

But I certainly appreciate the opportunity to address you today. My thanks to the FERC commissioners for inviting all of us here. I'm particularly interested in

some of the remarks made by Mr. Chairman in his opening remarks. I think his comments were essentially that it was time to see if we can quite talking the talk in the Southwest and start walking the walk. But I think we're pretty mindful with events from the market happenings in the entire western interconnection over the past couple of years that we certainly think we need to walk before we can run and take our time getting started. There are some pretty dire consequences out there.

And the other fact is that I think we need to talk enough to know which direction we ought to start walking because if we step off the curb and get run over immediately it's not going to do us any good either. So I hear the sense of urgency to move forward but I think we need to be in the right direction as well.

(Slide.)

A couple of topics that I'm going to cover sprinkled throughout my talk today are here I want to give you all some background on WestConnect and the major initiatives that we've initiated over the past couple of years, talk a little bit about the status in light of the White Paper and the White Paper issues. Mr. Chairman had also mentioned some of those issues so you've got a highlight of I think where some of the differences are from what we're proposing and from what is viewed in the White

Paper and also where we intend to go from here as we move forward with RTO formation in this part of the country.

(Slide.)

Some of the initiatives of the past several years, certainly it was no mean task for all of you who spent many, many hours in various rooms around Phoenix and throughout New Mexico, Texas, El Paso in the early years trying to form DesertSTAR and then WestConnect. A major initiative and a major achievement over the past several years was simply creating and filing the document that we submitted to FERC a couple of years ago.

More recently since we filed our request for a declaratory order we have since joined with both California ISO and the RTO West folks in the Pacific Northwest in an intensive effort to help resolves seams issues, smooth out the rough edges in the different market designs that we are developing throughout the Western Interconnection.

More recently we have initiated a cost/benefit analysis here in the greater Desert Southwest area. I apologize, I'm probably going to slip and say Desert Southwest many times. We're actually expanding the scope in that cost/benefit analysis to the high plains, the Rocky Mountain area, Desert Southwest, Great Basin and Imperial Valley of California. So we are the southern part of the Western Interconnection as well as we are Desert

Southwest.

And then finally I'm going to walk you through our exploration of the phased-in approach for RTO functionality here.

Our efforts to create an RTO, Commissioner Massey was correct pretty generally in the time frame, we started in 1997 trying to form DesertSTAR. Again that's the old terminology, Desert Southwest Transmission and Reliability Operator. The conversation was to WestConnect in 2001 primarily to create a for profit transmission company and RTO. And our request for a declaratory order was filed with FERC about two years ago.

(Slide.)

There was obviously a lengthy stakeholder process that we went through to develop the market design that was filed. It was broadly accepted by FERC in its order back to the WestConnect participants about a year ago. We've had a couple of additional requests for enlightenment on that order and the most recent of which was addressed a couple of weeks ago.

I'll tell you a little later there were several key market design elements within that proposal that were not approved by the FERC and they're pretty critical to a lot of the participants here in our original proposal.

(Slide.)

Our WestConnect participants are listed here. We have four investor-owned utilities who actually made the filing in from of FERC. We have three additional non-FERC jurisdictional entities you see on the bottom that are participating in the process. We've got a little bit different funding as you see in the graphic there as well.

The one thing to stress here is behind this slide you don't really see it but as to the four investor-owned on the top part of this screen and the non-FERC jurisdictional entities on the bottom, the amount of transmission assets owned by the two groups is split roughly 50/50 whether you count transmission miles or transmission investment. So the non-FERC jurisdictionals own a significant amount of transmission in the area and they're pretty broadly viewed as being critical to have the non-FERC jurisdictional entities involved in order to have a complete market in this part of the Western Interconnection.

(Slide.)

As I mentioned, WestConnect did file with FERC. An order was returned on October 10, 2002. I discovered a typo in the handouts so you can correct that as you see fit. But FERC generally approved many areas of WestConnect's filing. The governance structure, board selection process with a few tweaks were approved. Physical rights congestion management model was approved within a subsequent order that was backed

off a little bit as a day one concept.

We have a transmission adjustment component which is necessary for Western Area Power Administration's participants. That was adjusted as well. And FERC also requested some additional information on certain design elements within that proposal.

(Slide.)

But FERC did not approve some of the key elements that were thought to be extremely necessary for the broad transmission owner representation for all of the folks that I showed on the previous slide.

One of the things that were not addressed, there was a suit of transmission owner rights contained in our transmission control agreement, essentially the contract between the transmission owners and the RTO as an operator of those assets. Those are very critical to a lot of the owners.

Embedded within that is the concept of whether or not that control contract between the owner and the RTO has primacy over the tariff and that the benefit of that bargain prevails or whether those can be changed with tariff filings by a broader stakeholder group.

The congestion management proposal that was made is critical for most folks to extend beyond the initial operations date. I think the fact that it's considered to

be a day one date without any definition of what day one is causes some angst among folks.

FTRs for native load past day one is also critical. That was clarified somewhat in the order that we received recently. But there I think remain a few issues still to talk through.

And certainly a right of first refusal for transmission owners to build critical new infrastructure on the facilities that they have built in the past that they may have some financial obligations and essentially some liens against are also critical.

As I said just a minute ago a lot of these elements are very critical for securing and ensuring the non-FERC jurisdictional entities ongoing participation in WestConnect.

Moving a little bit now into some other areas that we are exploring and moving on in WestConnect, recently DOE performed a cost/benefit analysis which was instructive in that it did not show a net benefit for most entities in the Southwest part of the country. We certainly want to explore that a little further, see what the exact impacts are on a state by state basis and possibly a company by company basis.

(Slide.)

We embarked on a cost/benefit analysis earlier this

year in the late spring as we started putting together a group of folks to move forward on this. The effort includes 16 study participants so it is broader than the seven that I showed you on the slide a moment ago.

We intend to assess the costs and benefits of markets in the Southwest and the greater area, the southern western interconnection both with and without WestConnect in effect.

And we also are attempting to assess the costs and benefits of the various phases of RTO functionality that we intend or are proposing to implement to see what the costs benefits of those implementation efforts might be.

(Slide.)

I'm showing here the study participants that we have for the cost/benefits study. The key here, those in black are the original seven WestConnect proponents that we've had on board for quite a while. You can see here of the other nine we've got quite a mix of new entities participating in our cost/benefit analysis.

I think a critical thing that strikes me here as well, as you add these new entities to the mix we don't appreciably change our 50/50 ratio of FERC jurisdiction to non-jurisdictional transmission assets. So even with greater participation I think we're still in the position where we have a tremendous quantity of non-FERC

jurisdictional transmission in our proposed marketplace.

(Slide.)

This is an overview of some topics I intend to cover in a little more detail in a minute. But our phased approach, just as a preview, we currently have three phases identified.

Phase 1 is the creation of a common OASIS system with energy trading bulletin board. You're going to hear quite a bit more from the next speaker as David Wiggs outlines the westTTrans concept.

Our second phase is to move into a grid-wide transmission tariff, a little more formal congestion management system or scheme that we think we can have some indication of congestion management and market clearing price indication in our Phase 1. But we intend to get more formal in Phase 2.

Phase 3 would be the full and final implementation of an RTO when it makes sense to do so.

One thing to note is for some of you that have seen previous presentation we originally last spring had four phases that we were proposing. We found that the technology was ahead of us and we combined our original first two phases into this current Phase 1. So as we've gotten into this approach we've found that we're a little more efficient than we thought we might be.

(Slide.)

Again going back to part of the reason for this conference to compare and contrast the standard market design and the wholesale market platform, FERC did issue additional information in April of this year . It is their latest direction on market design. We note that there are some significant differences from the standard market design that was originally proposed.

And key to this, and again it was noted earlier in the conference, the ability to have regional variation to craft a market that works for the specific regions we think makes eminent sense. And that is exactly what we are proposing for this area.

And again, the cost justification of the efforts I think is also critical. It simply doesn't make sense to create a market design at any cost. I think it makes much more sense to create a market design that works at a reasonable cost.

(Slide.)

Some of the issues raised in FERC's wholesale market platform design. I'm going to go fairly quickly through these because at our stage of implementation it's very difficult to contrast where WestConnect stands. We're still trying to come up with the first functionality of an RTO. We really don't fit in with development and I don't

intend to report on each and every step.

But I think some of these are worth noting. Number three here dealing with independent market monitors, we are actively participating in the SSG-WI process as well as the CRPSE and Western Governors' process along with OMLI and FERC on dealing with market monitoring and mitigation mechanisms for the west. So we think that's ongoing.

Frankly, that can probably be in place before RTOs. I don't think it has to wait for an RTO to be in place.

(Slide.)

Some more tariff administration and design issues. Note on here item six, that is also a subject of the SSG-WI work group. We're trying to deal with export fees that are proposed in the three markets.

(Slide.)

Some other White Paper issues, interregional coordination. I indicates that WestConnect is certainly a full participant in the SSG-WI process.

(Slide.)

Coming on down to another key one I think in this region, transmission planning. We fully support regional and subregional transmission planning efforts. SSG-WI is nearing completion of its initial 10-year transmission expansion plan. The folks in that work group are coming up and trying to make sure they all understand the conclusions

from that study.

A little closer to home there has been a central Arizona transmission study performed for expansion facilities here in Arizona. That has been expanded across the river into California. And note that in a couple of days Wyoming and Utah are having a session to create their own subregional planning process there.

We certainly believe that we need to continue efforts in all the areas, subregional and interconnection-wide, to make sure that the transmission grid is robust enough to handle the markets that we want to set up.

(Slide.)

Having gone through that, given the wholesale market platform issuance by FERC the WestConnect entities and transmission owners in reassessing what they received by way of an order from FERC, looking at the wholesale market platform White Paper, certainly had some concerns. As I mentioned a couple of times, there is a major presence of non-FERC jurisdictional transmission owners within the region.

We also have tried to create the market design in the WestConnect structure through a process of consensus and collaboration amount all of the transmission owners. We certainly want them all involved. In order to do so we need to accommodate the needs of the different types of

transmission owners.

This may not be the right word, the but the "takeaways" from FERC within the WestConnect design as I indicate don an earlier slide certainly has slowed our forward momentum. Folks are wondering just what's left. If congestion management, for example, is only there for a short period of time what does that mean in the overall commitment of a transmission owner to move forward with that market design?

Additionally, given the experience in the Western Interconnection, particularly in the California market, an SMD-like market with centralized energy markets run by the RTO is not typically viewed as necessary or cost justified here in the Southwest. We think the cost/benefit analysis will shed some additional light on that for us.

And, lastly, there are some very large implementation costs and it takes a lot of time to put a full RTO together.

(Slide.)

Given those concerns, the transmission owners have been reassessing how they would like to proceed with RTO implementation. We think initially that the functionality that's put in place needs to show some benefits to the system, to the users of the transmission system while keeping costs and benefits in proportion and justifiable.

We find that many of the issues surrounding RTO formation are very contentious within the multiple state jurisdictions that we're dealing with here. Those issues need to be resolved with due deliberation, not necessarily with haste, to make sure that all the state commissions are on board as well as also the various types of transmission owners we have.

We think building incrementally on what has worked today, echoing Commissioner Lovejoy's comments, it's not necessarily broken for the way the market is operating in the Southwest today. There are places that need to be improved. We need to add incrementally to that.

And we see interest in the phased-in approach growing, and that includes a lot of transmission owners who are not within the original footprint of the seven utilities who filed the WestConnect RTO approach.

(Slide.)

Some of our key principles in approaching a phased-in functionality for a market in this area:

We would initially implement those wholesale transmission elements that add value to end users.

We would certainly like to defer low benefit/high cost items as long as possible. If they're not justifiable maybe they don't need to be implemented at all.

Creating a full-blown RTO organization, hiring

staff we think needs to be deferred until it is cost justified.

And we also believe that the elements, market elements ought to be brought online as they are justified, not necessarily waiting until you've got the full RTO in place.

(Slide.)

Again a little more expansion on a previous slide. This is a timeline type graph of what we believe is doable on an implementation approach. As I mentioned, we've already discovered that we can compress part of the schedule. And we took an originally two phases, moved them into Phase 1.

The WestConnect folks fully support the westTTrans effort. But I think we also -- and you're going to hear about that in a few minutes -- but we also believe that some of these elements will provide some additional functionality for the WestConnect participants over and above what westTTrans does. We certainly believe and agree on the benefits and the functionality of the core OASIS system as providing full visibility to market participants in the use of a transmission system. But we certainly see some added enhancements in an energy bulletin board, potentially some congestion management clearing bids put on that system. And that would then allow us to springboard from that into more

formal congestion management in our Phase 2.

One other thing I'd like to say is that among the WestConnect participants they are looking at commitments to any specific phase of this phased in approach as a single commitment buying into a Phase 1, for example, is not seen as committing any of the entities to moving on into Phases 2 and 3.

Again as I mentioned earlier as move forward across this draft we get more and more formal in the processes and functionality that is being performed by the RTO or by the entities implementing the RTO functionality.

Phase 3 would be implementing the full RTO.

(Slide.)

All of this presents some opportunities as well as some issues. Certainly as additional, as we get farther along the process we're going to find things we missed. There may be other functions that we can add in. We may be changing as we go. We certainly hope we can adapt to those as we identify those areas.

I think as seen by melding our original Phase 1 and Phase 2, the participants that we have so far certainly intend to remain flexible and willing to make changes around the edges of this original concept and do what is needed.

We heard earlier there is a concern about the independence of this effort. We certainly recognize FERC's

desires are to have independent governance and leadership of this effort sooner rather than later. We've thought of some options that we need to explore of ways that we can try to get that independent oversight, whether it's through an audit function or some other means of providing the oversight that would make FERC comfortable with this effort.

And again, the seams efforts need to continue. We fully intend to support the SSG-WI process in the West and eliminate as many of the rough edges as we can through that process.

(Slide.)

Where we are now. We are continuing seams efforts, as I've alluded to several times in here. The planning effort is underway, it will be producing a 10-year plan within the next couple of months.

Congestion management efforts, trying to meld the three different congestion management proposals of RTO West, California ISO and WestConnect, is working hard to find ways to make those fit together and provide meaningful information back to all of its participants.

Market monitoring is ongoing we think because certainly some low hanging fruit there that may be implementable prior to RTO formation.

Our cost benefit analysis is underway. We're a little slower than we anticipated and we're not going to

make it by the end of this year with results. We anticipate those in first quarter of next year.

And as you will hear in a minute, the OASIS and our Phase 1 implementation is also underway and we also expect that to be operable the first quarter of next year.

(Slide.)

Ongoing from here, we've got to complete the cost/benefit analysis as well as continue whatever encouragement WestConnect can put into the common OASIS process. That is essentially a function of the individual transmission owners, not WestConnect itself. But it's critical. I believe it's needed, it's necessary and it's doable now.

We will continue to search for in the functionality that makes sense and to implement RTO functionality in phases as the opportunities arise and form a fullblown RTO here in the southern part of the Western Interconnection when it's cost-effective to do so.

(Slide.)

And that's my remarks this morning. So thank you very much.

STATEMENT OF DAVID WIGGS, GENERAL MANAGER, LOS ANGELES DEPARTMENT OF WATER AND POWER

MR. WIGGS: I think I'm just going to stay seated. And, Charlie, if you could just flip to the next one.

(Slide.)

Good morning. I will try to do this while I'm sitting down. Again, Mr. Chairman, Commissioners, appreciate the opportunity to be here.

You know, in my prior investor-owned life both as a lawyer and a CEO I appeared before a forum of FERC many, many times. But as a public power utility it's very rare that I would appear before a quorum of the FERC. With all due respect, Mr. Chairman, I'd just assume keep it that way as I go forward.

(Laughter.)

I also want to say to our state commissioners, Los Angeles had nothing to do with the California deregulation mess. In fact, we were fortunate to stay out of that. And I say it has formed the basis of a lot of our beliefs on this and what we're going forward with.

(Slide.)

But I wanted to do today was take the opportunity to present an overview of what public power entities in the West have been doing to improve wholesale markets and benefit their customers. My message is meant to convey two basic points: first, that public power can participate and even lead in improving wholesale markets in the West where we do own approximately 50 percent of the transmission facilities.

And, secondly, that the improvements to the wholesale market can be achieved on a voluntary basis that allows us to protect public power submission to provide reliable and economic electricity tot our customers.

We believe in the West that bilateral wholesale electric markets work well. While they may not be textbook perfect, public power believes the best way to improve the wholesale market is in a voluntary manner with measured and incremental steps. One very significant important step is westTTrans.

The LADWP that serves almost 4 million people and owns about 28 percent of the import transmission capacity in California has joined a very extensive and impressive group of other transmission owners and operators to create a single independently operated common OASIS. This common OASIS, westTTrans, will not only in our view make the wholesale market in the West more competitive and efficient but it will also allow us to maintain control and ownership of our core transmission assets.

What I want to do is just going to give you a little brief history and who's involved and talk a little bit about what we're trying to do.

(Slide.)

Initially this started as a public power initiative of the West, PPIW. It was a voluntary coalition of large

public power agencies working to provide benefits to the customers, enhance transmission access, ensure reliability, support competitive, bilateral, wholesale markets but work within the existing regulatory structure, and preserve the individual business models.

The initial members included ourselves as well as IID, SMD in California, SRP, Southwestern Transmission Coop, Tri-State G&T and WAPA.

(Slide.)

And basically what it is, and Charlie has already alluded to this, it is a common internet site for posting and reserving transmission in a large portion of the West operated by an independent third party.

We think it's a cost-effective way, means to enhance transmission access. We think it's a way to modernize transmission OASIS reservations involving multiple transmission providers.

It will be available to all market participants.

And, as Charlie said, it's scheduled to be operational by the first quarter of next year.

So what we're doing is eliminating multiple OASIS sites. We're replacing it with one common site. Now you can query multiple providers across a very large region in one place with standardized software user interface. But we have not affected the native load priorities of public

power. There is no transfer or ownership or control of the transmission.

The third party group that will run this for us is a software company OATI, I think well-known in the industry, and they're developing the software and will operate it.

(Slide.)

The participating organizations, as we've discussed a little bit, it started with the public power initiative. The WestConnect group was then added, as Charlie has talked about. And we've also talked to additional western utilities that have joined this effort.

In fact, if you look at the map this covers a very significant portion of the western market. Obviously we won't include Texas and the eastern part of Nebraska. But we do believe that eventually we will get the rest of the Northwest utilities and that this entire map will be in the blue. This, of course, will always be done on a voluntary basis and asking them to join.

(Slide.)

Here is the group of utilities involved. You will note that it's all varieties from investor-owned to municipals to coops. Again, we have letters of -- contracts or signed letters of intent from all of these entities with our vendor. And we will continue to add new utilities to this.

If you take a look, as I said, LADWP has about 28 percent of the import, percentage of the import transmission in California. If you add the other utilities from California this will include close to 50 percent of the transmission import case load in California. And of the whole region while it doesn't cover every part of it it covers a very, very large percentage of the transmission.

(Slide.)

We think the benefits of westTTrans are pretty straightforward. It helps us build upon existing open access transmission tariffs and existing bilateral energy markets.

It supports reliability by making transmission more easily available to deliver generation to loads.

It creates market efficiency through enhanced utilization of the regional transmission grid.

It provides workable tolls to support a viable secondary market for transmission.

And it provides a platform for additional market improvements through voluntary cooperation.

Now, what I want to say is this does a lot of things, a lot of benefit but clearly we understand it doesn't do everything. In my understand in talking to operators it will help smooth some of the seam issues. It does allow to post ancillary services on a common bulletin

board. We think it does improve reliability by providing us better and quicker access to all this data.

But it doesn't address pancaking of rates. It doesn't address or envision any kind of financial rights right now in transmission.

It certainly doesn't commit anyone to join an RTO but it doesn't prohibit that at all.

It doesn't even create a legal entity that has any kind of authority over anybody and it's not set up to be a policing organization or a market-monitoring organization

(Slide.)

What we do think, you know, it is a start. It's a good first step. We are looking at in the future that we will continue to pursue improve, pursue enhancements. I talked about some of those. We'll do it on a voluntary basis. We'll get feedback from everybody involved.

We think we can enhance the regional price transparency for bilateral wholesale markets for instance by creating a new market indices.

We want to standardize the electricity interchange scheduling to further minimize the seam issues.

We've designed bilateral market methods to increase efficient use of the transmission grid.

And we want to be able to support coordination of new transmission planning and expansion to interconnections

and operations.

And as I stated, we're not going to address all of the concerns yet. And we may never address all of the concerns the Commission has. But what we have done is try to take up the challenge the Chairman issued about doing something, moving forward, offering some kinds of alternatives and get serious about it and not just talk about it.

This will be operational next year. And we believe it does represent a cooperative effort between a very large and very diverse group of utilities that only control a vast amount of transmission that are willing to work together on a voluntary basis to improve the efficiency of the wholesale market without giving up the ownership that is so important to them for their native load requirements both now and in the future.

And let me digress just a moment from Los Angeles' perspective. We did not enter the deregulation. Some of it's by pure luck. Better be lucky than good sometimes. But from our customers' perspective they don't really know what happened.

What they do know is that their utility stayed a very integrated utility. They stayed in control of their transmission and their generation and their rates.

They know that because of that we had absolutely no

blackouts. We've had no rate increases. And in addition to that we're still spending billions of dollars on infrastructure. We're building new power plants. We're upgrading our transmission facilities.

We're a double-A rated utility. And to change that business, to change that basic structure there's simply of the 4 million people there is simply no political will or push to do that right now. It would be very difficult.

I kidded somebody, and I say this with a touch of humor, short of military takeover it is going to be very hard to move at this time where you give up that kind of control of your transmission facilities. But that's why we're so committed to this process to try to do it on a voluntary basis to achieve some of these market efficiencies that you do need and we think are appropriate without giving up that control or ownership at least right now

So, we look forward to keeping you advised about our process and our progress. We certainly want to hear from FERC on their ideas and their suggestions. May not always agree with all of them and may not always want to implement them but we certainly want to hear about them. And we certainly respect very much the work that FERC does.

So, again, thank you for being here. And we look forward to working with you in the future.

Charlie.

CHAIRMAN WOOD: David, on that OASIS site are those ATC amounts or how are they calculated? Are they just delivered from the utility or are they independently?

MR. WIGGS: You know let me get some of our technical folks up to answer specific questions. But Charlie may know. Do you know the answers to some of the specifics on our?

CHAIRMAN WOOD: Yeah, just whoever is working on the westTTrans.net.

MR. REINHOLD: What was your specific question again?

CHAIRMAN WOOD: Who is available transmission capacity?

MR. REINHOLD: Each utility will be supplying the total. The site itself then will generate the available based on usage that comes in is my understanding. Certainly there's lots of folks out here -- Okay.

MR. WIGGS: Yeah, that's correct. That's the way it was done. Basically it's just taking everybody's OASIS, and we calculate our own and put it on there, and then coordinate it in one spot where you can go one place and get all of that information at this point in time. That's my understanding. No one is going to come -- and eventually we may get to a point where we have somebody come are you sure you're doing what you're supposed to do or releasing

everything you should release? But right now it's still being done on a voluntary basis and relying on each utility to give that information. That's the way it works.

And we do have several people here, we may not want to do it right now, that have specifically designed this and have worked with it day in/day out that could help and respond to any specific questions.

CHAIRMAN WOOD: What kind of customer input has there been for this? Is this the kind of thing that people want or is this?

MR. WIGGS: Well, as I said, in Los Angeles what they want is basically to be left alone. But what they accept is that over time we are trying to improve the wholesale markets. You know, the promise of as you say in the gas industry eventually got some lower prices, but that promise has been heard in California before and nobody's real interested anymore. So what they want us to do is continue to keep our rates where they are and keep our reliability where they are. But if we can work in the wholesale markets to improve that and be able to bring in power better or lower costs then certainly they'd be in favor of that.

But they're not going to be in favor of giving up ownership of that early on until they can see some sustained benefits over the country. Now, eventually if things begin

to really pick up as you believe and there's a lot of good sustained benefits for a majority of customers then clearly we want to continue to pursue that. But right now we really want to do it on an incremental basis and a very cautious basis. We're simply not risk takers right now. We've been there and so we're just not going to do that.

CHAIRMAN WOOD: Let me kind of leverage back into the presentation Charlie made. I'm back on the independence issue I raised in my opening comments which is I certainly appreciate the steps that are being taken here. I guess my expectations were kind of set by the original proposal of WestConnect that we've now gone through a couple iterations on trying to get clear on.

And I'm trying to resist part of the urge to view this as a step backwards when I looked at kind of where you had laid out the vision for going down here and some of the customized approaches that I think with some effort we have come around on at our Commission to agree should meet the broader issues of a good, fair, open market.

And I'm sitting next to a guy who set up the ERCOT market. And I remember when we were there it was about, oh, about a \$4 or \$5 million a year enterprise to have an independently operated, pretty streamdowned I guess RTO, ISO, whatever we want to call it over that market there. And I wonder has NERC, certainly the NERC security

coordination responsibilities that we have across the country which we're familiar with, a regional planning process, a regional tariff to make sure that those transmission projects got paid for, and OASIS one-stop shop approach there.

And I'm wondering why have the WestConnect TOs kind of pulled back from really doing what our -- independence is pretty cheap. Assume the day-ahead market and all this stuff that can get you over 100 million bucks perhaps. But I'm wondering what's kind of been the dynamic among the discussion in the WestConnect group in that regard up to now?

MR. REINHOLD: Well, first of all, our experience in looking at the functionality that would be necessary and the infrastructure to put an RTO together our cost estimates are more in the \$150 million range than the \$4 to \$5 million range that you mentioned.

CHAIRMAN WOOD: That's your RTO with day-ahead markets and transmission rights?

MR. REINHOLD: That is the RTO approach as filed.

CHAIRMAN WOOD: Okay.

MR. REINHOLD: And WestConnect did not anticipate operating a day-ahead market. So the market operations addition is an incremental cost. It may be -- there's been some debate as to whether that's a large cost or a small

incremental cost to the general RTO operations.

But in going through a lengthy process and putting together a specification for what it would take to implement WestConnect we came up with a significant dollar investment. That gave pause. It certainly had our jurisdictional entities going back to their local regulators, whoever they may be, the states or the local self-regulated entity, wondering if that was the right way to go, whether the truly beneficial functionalities of an RTO can be implemented ahead of investing those dollars to have the entire RTO up and running at one time.

And the approach is, the comfort level is that we need to begin implementing RTO functionality as we can at the lower cost and defer that \$150 million to implement the entire RTO.

CHAIRMAN WOOD: That's fair. But I guess I don't want you all or us to be or anybody in the audience to think that having a regional planning process with a tariff to recover those costs is a \$150 million a year enterprise.

MR. REINHOLD: It is not. It is not. In essence that is the company structure, the RTO itself, to create the company and the employees and the building and the computers.

CHAIRMAN WOOD: Again, I would just suggest look immediately to the west for a good comparative number on

that.

MR. REINHOLD: But as for planning, we're participating in planning right now. We think that's something that we don't need to --

CHAIRMAN WOOD: Do you have a tariff to recover the costs of the planning?

MR. REINHOLD: We do not have a WestConnect-wide type tariff. The recovery is up to the individual transmission owners at this point.

CHAIRMAN WOOD: I mean I think we've seen just looking around the country that that, once that mechanism is up for costs to be recovered then TOs are a lot more inclined to want to build because they know they can get the money back.

MR. REINHOLD: Okay.

CHAIRMAN WOOD: What can, clearly the SSG-WI process and others have generated a lot of ideas. Our staff has been involved in that. You've been involved in that. Who will be the entity here, if the independent board's contemplated to be on the backend who will be the independent entity here in the Southwest that then makes those -- or takes that work product and makes decisions? Because I think that's what SSG-WI was suppose to do is give the report back to RTO West, to Cal. ISO and to WestConnect to them make the decisions to go forward.

MR. REINHOLD: Correct. At this point WestConnect is participating in the SSG-WI process through the transmission sponsors of WestConnect. So it is an informal organization of those transmission owners pursuing the SSG-WI process.

And we've talked about some addition always to provide some additional independence to that process whether it's an audit mechanism to have a third party insure the decision making process and the motivations behind the decisions or whether there is some other surrogate short of the full separate entity and organization.

COMMISSIONER BROWNELL: I have an idea and a question. The issue of cost has been one that we've encountered in all of our discussions out here. And it seems odd to me that we have a \$5 million cost to get the basic functionality in Texas and a \$150 million to do the same thing here. It would suggest to me we're not talking about the same thing.

I wonder if my fellow commissioners both at the FERC and the states would think it might be a good idea to put together a team of staff to go over basically those four or five functions that you talked about, Pat, and go over the budget that you have proposed which I actually haven't seen so I can't really speak to it, and find out where that disconnect is so that the commissioners who are being asked

to make these decisions have kind of an independent verification of the costs?

I don't know how you're feel about that.

Chairman Spitzer? Well, why don't we pursue that offline.

Oh, here's Chairman Spitzer.

MR. SPITZER: Any work that could be done to assure that we've got apples to apples comparison I think would be very helpful. A lot of the information I've seen is, particularly the DOE is projections. And there's short-run projection, long-run projections. You know, I've been in accounting long enough to know I'd like to see some common parameters and I think more work would certainly be helpful to assure that --

COMMISSIONER BROWNELL: Good.

MR. SPITZER: -- the ratepayers get some value for whatever undertaking we've embarked upon.

COMMISSIONER BROWNELL: Good.

And I think there are two aspects of that. One of the things that I suggested to most of the market participants last week was that people doing the cost/benefit study actually talk to the people at DOE and our shop and our consultants to make sure it's a fully robust study. One of the things that I think we all know, and Chairman Spitzer being in accounting knows this probably

better than I, a cost/benefit can do many things but it doesn't do everything. And to get a fully robust study I think you want to talk to people who would -- I think there are questions we would ask today that we wouldn't.

I think the second aspect is putting together a staff team to really go over those numbers and functionality.

But my question is this: I'm not sure, you talk a lot about California, I actually thought you did participate in the wholesale and did pretty well at LADWP. I could be wrong.

(Laughter.)

I don't know how this prevents, the question is this, Mr. Wiggs and Mr. Reinhold, I don't see how this gets us to that planning function which ultimately builds a system that prevents some of the fragility that we saw that exacerbated the western market. And I don't really understand how it gets to a set of rules that actually protects the neighbors and protects the customers of California.

So if you could explain to me how we get there? Because I think that's part of our sense of urgency.

MR. WIGGS: Well, first let me of course respond a little bit to the California energy crisis. It was before I was there so I had no reason not to do anything but looking

to see if DWP did anything they weren't supposed to do. And as it turns out they did not. And while it's still pending before your Commission the trial staff has recommended none of that, drop all of those proceedings against the department for anything to do with improper sales.

They did step up. We clearly stepped up because we had surplus capacity and we sold it to California first and kept lights on in a significant part of the rest of the state because we had that ability to do that. But there was nothing improper done that I could fine.

COMMISSIONER BROWNELL: Wasn't suggesting there was.

MR. WIGGS: Hmm? Okay.

COMMISSIONER BROWNELL: I was not suggesting there was.

MR. WIGGS: And again that's, you know, the reason we have -- and the Chairman asked earlier feedback from our customers as to what they want -- our customer rates have never been higher. They've gone from 64 percent to over 85 percent on even your residential rates. What we found was that while price is very important it's not as important as reliability and predictability.

And so that what we are seeing is simply just go slowly, let's see what we can do, let's see if these markets can improve our situation, but don't, don't take any steps

to change our basic business model right now.

The other question, well if I start it right now I don't -- you may want to, did you have something?

MR. REINHOLD: Yeah. I'd like to add that on planning there is planning underway throughout the Western Interconnection both subregionally and Western Interconnection-wide. And there are facilities being built, new facilities here in the Southwest. There are facilities being built in the Northwest. Many of them are identified during the California market crisis as bottlenecks on the system. They are being built to alleviate and relieve some of those congestion points.

So entities are finding ways to build transmission without an interconnection-wide or region-wide tariff for cost recovery. So efforts are underway. Certainly there's undoubtedly ways that we could improve on the process through SSG-WI. We're certainly trying to identify some of the broader interconnection-wide picture that we received. And I think time will tell as that first transmission study comes out soon, we'll see if it hits the mark. And the next couple of iterations can improve on that.

MR. WIGGS: I do know at DWP we are in fact investing several hundreds of million dollars in a very major upgrade of a DC line from northern California down with Southern California Edison as our partner and

Bonneville Power to be sure we have strengthened the system and upgrading that line. One of the things we're doing right now.

COMMISSIONER BROWNELL: And I appreciate the work that's been done on planning. But I have to tell you when talking to the companies who are building and when talking to the folks on Wall Street the lack of transparency and independence in that planning process and the lack of the consistent set of rules is making that building difficult.

So I think indeed some things are getting done. I talked to a couple of people who are here today actually who talked about delays in a project because of inconsistent rules and because of financing. One in one case it was \$10 to \$20 million of extra cost because of the delay.

So, yes, things are being built but I'm not sure about the timeliness and efficiency or the robustness of the system that we're building.

MR. WIGGS: Yeah, I agree 100 percent with that. What I have seen and in my life have raised a huge amount of money on Wall Street. And nobody wants to come into California with any money right now because it is totally uncertain, nobody knows what's going to happen. The capital markets don't like uncertainty. They're not going to put money into it.

So we agree that we should get to a set of rules

that give some certainty where the market can raise the money it needs to raise to build the infrastructure. Agree 100 percent with that.

COMMISSIONER BROWNELL: Thank you.

CHAIRMAN WOOD: Any questions? Anybody in the audience?

MR. WIGGS: Okay, we get to go back. We're done. Thank you, Mr. Chairman, Commissioners.

MS. MCKINLEY: I believe it's time for lunch. And I'm Sarah McKinley with FERC. And I just wanted to make a brief announcement about the luncheon arrangements.

The hotel here has two restaurants on property and each one can handle about 100 people. And we have about 200 people here. So they've asked us if they can send half to one and half to the other and you can choose.

The Lantana has a, they set up a special buffet, a \$9.95 buffet with prime rib and seafood and soup and so forth. And to get to the Lantana you go out these doors, go to the elevator, straight ahead to the elevator, you go down to the first floor, out the front door. The Lantana is across the street and to the right.

Now, the other restaurant is called the Hole-in-the-Wall. It's in the back of this property. But to get there, to facilitate the hotel is setting up a little jitney buss right in the front of this building. So again you go

down to the first floor, go out the front, there will be a little bus to take you around to the back of the property, the Hole-in-the-Wall, and they've set up an express lunch for \$6.95.

So we'll see you back here at 1:00 o'clock sharp.

(Whereupon, at 11:52 a.m., the conference was recessed, to reconvene this same day at 1:00 p.m.)

A F T E R N O O N S E S S I O N

(1:20 P.M.)

CHAIRMAN WOOD: Okay, thank you all very much. This afternoon our first panel will be the transmission owners panel. And to moderate that effort will be Steve Glaser from Tucson Electric. So I will turn it over to Steve.

OPENING STATEMENT OF STEVE GLASER, SENIOR VICE
PRESIDENT, TUCSON ELECTRIC POWER COMPANY

MR. GLASER: Thank you, Chairman Wood.

It's my pleasure to moderate this august group here of public and IOUs. We will see what they have to say given what happened this morning.

When I asked everybody on the panel for a bio and a summary most of them sent something back and said, well, we're going to wait to see what happens in the morning before we decide what to say in the afternoon. So we'll see what they have to say now.

We'll start first with Steve Wheeler. Congratulations, Steve, on a new job which is now executive vice president of customer service and regulation for Arizona Public Service. That includes customer service, transmission distribution, state and regulatory affairs. So now you get to go rid out in bucket trucks as well, so it's a lot of fun.

Prior to that Steve was an attorney. He didn't want me to say that. But he was an attorney for 27 years at Snell & Wilmer practicing in utilities law, among other things. Steve has also been on various boards, including the Fiesta Bowl Committee. And is a graduate of two colleges back east that he didn't want me to mention but they're Ivy League colleges.

With that I'll turn it over to Steve Wheeler.

STATEMENT OF STEVE WHEELER, SENIOR VICE PRESIDENT,
REGULATION, SYSTEM PLANNING & OPERATIONS, ARIZONA PUBLIC
SERVICE COMPANY

MR. WHEELER: Thanks for the great introduction, Steve.

And I have to tell you, we have dispensation to take our coats off. And that was a voluntary act that was suggested by Chairman Wood. And thank you very much.

I appreciate the opportunity to speak on behalf of the funding investor-owned utilities that are part of WestConnect, and that is Arizona Public Service Company, Tucson Electric, El Paso Electric and Public Service Company of New Mexico. If I say anything particularly insightful or pleasing to your ears it is on behalf of all of them. If I say something inordinately stupid or jarring, again it is my fault, I beg your pardon and I'm speaking only individually.

And I'd like to start by first thanking you for

visiting us. That means a lot to have you out here on our home turf. Thank you also for listening to us with real concern and interest. And thank you also for the responsiveness we've seen today on the concerns that we do have as we work through standard market design and RTOs. You've given us condition approval of various aspects of WestConnect. You've modified the standard market design in your April White Paper to endorse the concept of flexibility and cost efficiency.

And you've also recognized our need for native load protection or at least measures designed to do that in the most recent rehearing order you gave us on WestConnect. And I thank you for that.

We as the IOUs in WestConnect support the goals of a workable, robust wholesale market that are the goals of both your SMD and RTO initiative. But we think that could be best achieved through voluntary regional cooperative efforts that involve all the parties, particularly our public power brethren. And that that also can be best achieved through very targeted, limited regulation that provides real value to our customers and that also provides stability to our business.

And that's why we spent thousands of dollars and literally millions of dollars forming WestConnect and its predecessor DesertSTAR. That's why we've been engaged in an

aggressive outreach program to bring in additional utilities outside of the WestConnect footprint. That's why we formed regional alliances. It's why we've now reconfigured some of the staging of the WestConnect functions in the manner that Charlie Reinhold described. And it's also why we're investing millions of dollars in new infrastructure.

During this entire debate it's almost become an article of faith that the transmission system is so aged and so tasked and that the wholesale market is so dysfunctional that only radical surgery through federal and state intervention can save us. And I would suggest to you that may be true in some areas of the country but it is not necessarily so in the Southwest.

And while I fully subscribe to Chairman Spitzer's concept of healthy tension, I would also ask you to consider a concept of proportionality. And by that I mean to examine whether or not the actions that you would have us take fit our particular circumstances and are necessary to address the problems that exist.

And in looking at the concept of proportionality I would suggest to you you can look at five different questions. The first would be is our area characterized by the type of gridlock congestion that you have seen and observed sometimes in the East? And I would suggest to you the answer is no.

On our system, the APS system, our most congested path which I think may even be the most congested path in the WestConnect footprint which is coming from Four Corners down to Phoenix, we have had to implement the congestion management system adopted by WECC only three-tenths of 1 percent of the time in the nine years it's been in place. And so I would suggest to you that congestion is not itself a problem that is similar to what you've seen in other areas of the country.

Another legitimate area of inquiry could be are we seeing progress retarded by moribund regulation at the state level? And I can tell you in Arizona that's certainly not the case. Our state commission is I think one of the most active in the country in promoting infrastructure development, in trying to see the wholesale market development develop, in advancing the different business models that you saw Chairman Spitzer talk about. They have a successful record of siting both generation and transmission lines. They have a staff that actively monitors transmission planning. And they have a statutory review process for it. So you are seeing a lot of supportive state regulatory activity.

Another legitimate area of inquiry is do you see infrastructure development lagging? And again using Arizona as an example I would say no. Since 1999 you've seen

upwards of 10,000 megawatts of new generation sited and constructed in our state both by utilities and by merchant generators.

In APS' case over the 10-year period 1999 through 2008 we will be investing over \$800 million in new transmission, an amount which will more than double our rate base in transmission assets.

Another legitimate question is, is our region balkanized by isolated systems that do not coordinate and work together? And, again, if you take a look at the activities that Charlie has talked about, if you recall David Wiggs' presentation on the broad scope of coordinated activity there you will see that's not the case.

But more importantly, if you look at the development of both generation and transmission in our area you'll see most of those are jointly owned projects where we have gotten together with our neighboring utilities and worked out jointly owned power plants, jointly owned transmission lines, reserve sharing arrangements. And we work under a very centralized and coordinated WECC.

And then, finally, are you seeing progress? Are you seeing cooperative efforts underway to improve the system? And again I hope that what you've seen today would suggest that we are taking steps both through outreach, both through dollars and through developing new systems to try to

make things even better.

In sum, we've taken steps that have avoided the disarray, the blackouts the price spikes that have characterized those regions which rushed pell-mell into untested market reform activities.

And I tell you these things not because we're looking for "attaboys" or trying to say that you can't make things better, but rather just to suggest to you that you go slow in adopting measures that may be considered unproductive or controversial that represent a flash cut change from the way we do business.

So I would ask of you if you say So what do you want us as federal regulators to do? I guess I would ask you to consider four things on behalf of us.

First, give us the flexibility that was promised in your April White Paper, the flexibility both in terms of time and in terms of structure to allow us to work on things that will address the particular needs we have and the different business models that are in the Southwest. Public power owns over half the generation, half the transmission and represent over half the load in the WestConnect footprint. We can't do it unless we have the public power needs, their legitimate needs addressed in a way that satisfies them.

So we ask you to be flexible in terms of structure

and timing.

We also ask you to be rigorous in the application of a cost/benefit test to make sure that what we are being asked to do provides real value to our customers and doesn't provide a fix that costs far more than the benefit it provides.

Third, I would suggest that because only APS and other transmission owners have at least the last stop legal obligation to serve our customers, since we're the ones who have to plan for and spend the money to make sure the lights are always on for our retail customers, please support and encourage measures which allow us to do that job.

And then, finally, we ask that you would continue to listen to and work with our state commissions as you have done in the past so that we have a harmonized system that does not subject us to conflicting mandates.

So I thank you again for listening to us. We look forward to continuing our efforts under your benevolent but hopefully lighthanded guidance. So thank you very much.

MR. GLASER: Thanks, Steve.

Next up we have David Areghini from the other large energy provider up here in the Valley, Salt River Project. Dave came to Salt River in 1990 and became the associate general manager of power, construction and engineering services in 1991. He's responsible for engineering,

construction, operations and the maintenance of the electric system.

He's a registered professional engineer in Arizona and California. Because before coming to Salt River Dave spent 18 years at that other large IOU, not LADWP but the other one in Los Angeles. Maybe we can have some discussions between Dave and Mr. Wiggs if he is around. No?

MR. AREGHINI: We both went the same direction.

MR. GLASER: That's true, you both did go the same direction.

Dave earned his Bachelor's Degree in engineering from the University of Arizona. And he has become very involved down south in our area with the College of Engineering and Mines and he's bringing some utility programs down to the University of Arizona. And we're appreciative of that. We hope to get some good students out of the program.

Additionally, Dave serves as president of the Rocky Mountain Electric League.

STATEMENT OF DAVID AREGHINI, ASSOCIATE GENERAL MANAGER,
POWER, CONSTRUCTION AND ENGINEERING SERVICES, SALT RIVER
PROJECT

MR. AREGHINI: Thank you, Steve.

I was getting a little nervous there at the end where you were going in my introduction when you got into my

academic background because I have two alma maters, one he mentioned, the University of Arizona, the other one U.C.L.A. And I was afraid that he was going to point out that their football team each allowed 59 points this last weekend.

Apparently, Steve spoke for the IOUs and apparently neither Ron nor I could be trusted to speak for the other, on the public, so we both are going to be given an opportunity here.

SRP, as Steve mentioned, is connected at the hip here with APS in that our service territory we have approximately 800,000 customers in Phoenix and we overlap. We are side by side with APS. We are very much connected.

I'm going to talk about and kind of enhance on some of the things Steve talked about, and that is the things that the publics and the privates have been able to do voluntarily and the successes we have. SRP is a system with its generation in remote areas primarily. And to bring that generation into our service territory obviously we have to have a lot of transmission.

Just about all that transmission is owned by a combination of utilities, some public, some private. That's gone on for the 50 years of growth that we have experienced here at SRP. And it has served us well and it has been very successful. And when there has been a need we have put our heads together and we have planned and we've implemented the

transmission and the generation that was needed by our retail systems.

Just recently Steve mention the number of megawatts that have been built in Arizona. Two or three years ago we, like many around the country, were panicked about meeting our summer peak load. And in Arizona the peak in the summer which is obviously when we set our peaks are about twice what it is in the winter. So therefore we have to either build or we have to arrange for the capacity to meet that peak.

Well, we had over 5,000 merchant megawatts appear out at Palo Verde. SRP operates the Palo Verde transmission system. Now, there was no enticement by a market other than what those merchants perceived to be the market. There was no orchestrated planning. Those merchants obviously saw that there was a market here, a wholesale market, and they built.

We, as the operators of the Palo Verde transmission system along with the other owners added to the transmission system so that we could get that new generation to a market so we could take care of that. And it worked very well. And, again, there was no orchestrated planning effort.

Now, since then and towards the latter part of that construction it has been identified that there is a need for transmission, additional transmission in Arizona. The

utilities as well as the merchants and the regulators have put their heads together under a system called the CATS system or CATS process, the Central Arizona Transmission System Process, and as a result of that additional transmission has been built to accommodate some of the merchant generation and some of those that the integrated utilities are building. All again without any kind of an orchestrated planning effort, and I hesitate to say especially from the federal level.

So we, so I think we out here, as Steve said, have a way of dealing with our issues, planning for our future and implementing. We have a very favorable regulatory environment. Our siting process to my knowledge has never turned down a transmission line. They have not made them easy to site but they have been rigorous in their pursuit of a quality among the environmental elements, the communities and the utilities. But in the end transmission gets built.

To my knowledge with maybe one or two exceptions after it was apparent that we were going to be overbuilt in Arizona a generation, a merchant generation was not rejected. There were some rejected but it was apparent that we were getting a period of over capacity.

So, again, Arizona and this region have been able to take care of their needs without orchestration from the outside.

But let me just say you can always get better. And for that reason we, SRP, have been involved in WestConnect from day one. We were involved way back in the days of DesertSTAR because there still are some protocols and some things that can be done with the operation and posting of transmission that would improve the market that exists today. And for that reason we certainly support this step that is being taken with westTTrans. It is in my opinion the first significant, constructive effort that has taken place that will attempt to level the playing field on transmission availability.

We were very pleased to hear that in the White Paper that FERC is advocating that if you don't see something that is cost effective you need not go forward with it. And for that reason we are a part, as you saw this morning, of the many, the 16 utilities that are working on the cost/benefit study. It will be that that will drive our decisions into the future with respect to how much more of an involvement in WestConnect that we maintain.

Finally, if I could give our visitors some suggestions. And one that I have been impressed with, an organization I've been impressed with that I know Commissioner Wood has a lot to do with, and that is ERCOT. I would suggest that the WECC which is our regional reliability council which was the first to implement a

required reliability criteria with penalties attached to it, that we look to some of the other things that ERCOT has done, particularly in the planning area.

The little that I know about ERCOT, transmission gets planned, we identify who needs to build it, and they identify who needs to build it and it happens. And things go quite smoothly there. I would suggest that you use the WECC more as an overarching organization to do some of the things particularly that are being done by SSG-WI now. To be facetious, I think that group needs some adult supervision. But to make more things happen. And I think the WECC is the organization that can do that.

That's primarily my suggestions to you. You have an organization in effect, use its staff, use its people. There will be a new executive director shortly. And I think it can move things along in a constructive manner in balancing reliability and the investment.

With that, thank you.

MR. GLASER: Thanks, Steve.

I know I'm only supposed to moderate but I did want to follow up on one of Dave's points, siting of transmission in the state. From a personal standpoint and a company standpoint the Corporation Commission authorized a transmission line for Tucson Electric a couple years ago for reliability issues down south in Nogales, did it timely.

Boy, if you could give us any help with the federal government and the agencies there we would really appreciate it because that process has taken two years. And we had, actually we have EIS hearings tomorrow. So the coordination of federal agencies is something that to the extent the federal government can help us with in the state we certainly would appreciate that, speaking on behalf of Tucson Electric as well as some of the other panelists up here.

I couldn't help it, give me a microphone and I'll talk.

The next panelist is the third Steve on the panel, Steve Fausett from Tri-State G&T, senior vice president of transmission. Steve's primarily responsible for the operation, maintenance, engineering and the planning of Tri-State's transmission system.

Prior to joining Tri-State in 1997 Steve had a 25-year career in the federal government with the U.S. Bureau of Reclamation and the Western Area Power Administration. His tenure included positions in Colorado, Montana, South Dakota and ended up with the regional manager for the Rocky Mountain Region for Western.

Steve's a native of California and has a Bachelor of Science degree in electrical engineering from the University of Utah. And I don't know how their football

team did last week.

STATEMENT OF STEVE FAUSETT, SENIOR VICE PRESIDENT,
TRANSMISSION, TRI-STATE GENERATION AND TRANSMISSION

MR. FAUSETT: Thank you very much.

Once again I'd like to thank the Commission for honoring us with your presence today and listening to some of our concerns.

Tri-State always has an identity crisis. Many people don't know who we are. So just a little profile here. We serve 44 member systems, distribution REAs in four states, Nebraska, Wyoming, Colorado and New Mexico. We have assets generation, coal generation in about 1,600 megawatts that we own or purchase, a nice contract with our friends in Western Area Power Administration for 650 megawatts of hydro and 600 megawatts of gas and oil. About 5,000 miles of transmission lines and 135 substations.

In the expanded WestConnect footprint which includes the Rocky Mountain Region now, within that, within WestConnect we'd be the fourth largest entity by load, the first largest entity by service territory, and second or third by transmission. So we have a very definite interest in the success of RTO formation activity.

We have been active in the past. We have a corporate policy of supporting ISO or RTOs. We worked in IndeGO, DesertSTAR and we're active, while not a planning

entity we've been active with WestConnect and are participating in their cost/benefit study. And we will continue to support RTO formation efforts but we do have some concerns.

Our interests are that in addition to our own transmission assets we operate in five control areas in the four states, buy extensive transmission services from both IOUs and public power entities in those states.

I'd like to talk a little bit about, and once again I should clarify I'm really speaking for Tri-State and I think also for some of the other cooperative entities in the area. And Tom will have an opportunity to speak also.

The attributes of a successful RTO in the Western Interconnection, first of all we think it should allow for participation by all types of utilities, including traditional vertically integrated utilities of all sorts, IOUs, cooperative, municipal utilities, our federal PMA. And when I say this I not only thing that it should be inclusive, I think it can be inclusive given the flexibility and some of the proposals that we're now exploring in WestConnect.

Our primary concern of WestConnect or we think any RTOs should be the efficient, i.e. cost effective, and fair operation of the transmission system and the reliable operation of the transmission system. I think there would

be a new emphasis within the RTO formation effort toward reliability.

We can realize all sorts of consumer benefits through reduced cost and so forth but if we compromise reliability and get a 24-hour blackout over a multi-state area it wipes out a lot of the benefits to the end-use consumers.

We believe that you should provide, the RTO should provide for solid planning and expansion of the transmission system. And, more importantly, it should facilitate the development of the wholesale market activities without being the market. And we'll explain that a little bit later.

A solid business plan where the benefits exceed costs. And primarily it should benefit the end-use consumer. At the end of the day the end-use consumer should see improvements in their pricing and in their reliability.

Some of the core features that we think would be necessary to form a practical, what I call practical RTO for the West would be real time reliability monitoring using simple and straightforward operational procedures. And once again sustain the ability of those of us that have obligation to serve to deliver our owned generation to our own load.

And I think we need to realize that the vertically integrated utility whether it's public or privately owned in

the WestConnect footprint is probably going to be the market design of choice and of necessity for retail service. That shouldn't stop us from sustaining and forming a wholesale market that is robust.

To avoid some of the complexities we're a firm believer in the management of transmission congestion by physical rights which precludes then any requirement for real time markets, for RTO generation -- for the RTO to be involved in generation purchases for either energy imbalance, load following or congestion management.

The transmission pricing, and this has been a sticking point in the past but I think there's lots of room to move on it, should be equitable and should encourage transmission expansion. There should be an emphasis on cost minimization for the RTO. That includes staffing and infrastructure certainly associated with the RTO but it also includes the burdens on participating utilities and of all stakeholder classes in the RTO.

We've heard about the tremendous costs in Cal. ISO for just the ISO and then the unfortunate associated PX. But if you talked from what I understand there were considerable costs incurred by the three participating IOUs out there for infrastructure and staff just to support the procedures required by the ISO. So we'll be looking for that sort of relief in the formation of an RTO in the

Southwest.

And, lastly, we talked about governance, independent, stakeholder, whatever. We really don't have a dog in that fight either way. We can go independent, we can go stakeholder. But we would sure like to see enlightened governance.

In the corporate world we've seen now there are increasing requirements for people sitting on corporate boards to have some knowledge of accounting practice. It seems like a reasonable thing to do. In the RTO world we'd like to see people sitting on the board independent or stakeholder that have knowledge of the utility industry, all aspects of it and perhaps most importantly, the operation of the transmission system.

One thing I do believe that we should take a look at some of the myths surrounding proposals for standardized markets that really don't apply here in the West. Some of these have been talked about.

The first thing is that there are dysfunctional markets and with substantial problems to be solved.

We have reasonable rates, in fact some of the lowest rates in the country in the Western Interconnection. I don't think that we're failing that badly.

Secondly, merchant plants and power marketers will be the models for future power supply expansion.

I don't think that's the case out here at least.

Deregulation of retail markets will benefit consumers.

Financial transmission rights and LMP markets will cause new transmission to be built.

Rather we believe it to be the contrary, that it will reward scarcity and does not encourage new transmission.

Generation can be dispatched at will to relieve transmission congestion.

Once again this is a financial rights model or LMP. In our region we have a lot of pulverized coal units that cannot be moved well. The flexibility we used to enjoy with our hydro system doesn't exist anymore because of river constraints both on the Colorado and the Columbia. And have issues with gas transportation and storage as far as being able to start and stop even gas-fired generation on a dime.

Another myth is that cheaper generation is available in large amounts with significant price differences.

As we know in the Western Interconnection we're on natural gas almost 24/7/365. So there is not -- the coal units are operating at extremely high plant factors and there is not a lot of margin to finance RTO operations.

And lastly, the complex pricing and everything

associated with LMP can be automated and computerized and we'll all understand it.

I've tried. Believe me I've tried.

WestConnect is a good start. I'll go beyond that, it's an excellent start. We support the effort of WestConnect. We're participating in the cost/benefit analysis.

The phased-in approach is workable. We believe that you should learn in the developmental mode and not in the failure mode as we've seen other ISOs do.

It appeals to most utilities in the region, most if not all.

The White Paper supports this approach.

It provides a framework for regional planning and we can take the additional steps, the learn-as-you-go steps if they're cost-effective.

And being a cooperative I can't leave without a postscript and argument for postage stamp transmission pricing or something approximating that where all consumers share the cost of the shared transmission grid. It's simply to apply. There's no art form, no negotiation required.

And I believe that cost shifts in transmission which there will be some if we sharpen our pencils and draw a bright line as to what is transmission and what is not that those can be narrowed.

And, lastly, it does provide a reliable cost recovery mechanism for expansions to the grid.

I know I've gone on at some length and I apologize for that. Once again we appreciate the opportunity.

MR. GLASER: Thanks, Steve.

Next up is Tom Jones. Tom is the chief executive officer of the Grand Canyon State Electrical Cooperative Association up here in Phoenix. That's a regional trade association of 27 electric, water, natural gas and telephone utilities in Arizona, California, New Mexico and Utah. So we're lucky to have Tom here, he covers the gamut obviously.

Tom has a Bachelor's and a Master's degree from the University of Arizona down in Tucson. He serves on the Board of Directors of Touchstone Energy and Ruralized Services, Inc. And his past civic activities have included being a councilman and the mayor of the town of Marana which is a small town just north of Tucson. And he's also served on several state boards and commissions as well.

With that, Tom Jones.

STATEMENT OF TOM JONES, GRAND CANYON STATE ELECTRIC COOPERATIVE ASSOCIATION

MR. JONES: Thank you, Steve.

Generally when I'm introduced and finally stand up there's kind of a sigh in the room because they were expecting the other Tom Jones.

(Laughter.)

So I'm sorry about that.

There's a training technique for public speakers where you advise the speaker to picture the audience nude as a way to calm your apprehensions about speaking. I've always had difficulty about that. And I could say that if I were doing that in this room it would be a little scary.

So what I do is I practice my speeches in front of my dog Honey. She's a golden lab. The great thing about practicing your speech in front of a dog is that no matter what you say they will look at you with an approving glance like Gee, you must be the smartest human in the world, I agree with everything you're saying.

So I'm going to think of you as Honey as I go through my remarks.

(Laughter.)

Certainly the cooperatives support the very worthy goals of robust, wholesale electric markets and also the goals that have become more and more prominent for us in recent times here of reliability. I suppose that you are down to myself and to Ron Moulton here a little later to follow me to find someone who's going to tell you something different than what you've heard this morning. I'm going to disappoint you because I'm going to sing a lot of the same songs that have already been heard. I think you'll have to

wait maybe until the next panel to get a little bit of a different view of what's going on.

The coops also want to thank the Commissioners for arranging this event and giving us the opportunity to participate. And in a reaction to the White Paper, to also thank you for your willingness to realize the importance of understanding that there are regional differences across the country, that the notion of one size fits all in this marketplace may not be possible or wise. And also for recognizing in the White Paper the importance of justifying the costs of things we do.

This is especially important for us in the electric cooperative program. And I will focus most of my remarks around how we think on behalf of our consumer member owners their view is of what all of this is about.

In Arizona the cooperatives do own our transmission system. It's interconnected to the western grid. We have been involved with the open access development since 1997, first with DesertSTAR, as many of you, and now of course with WestConnect. And we have been very supportive of all of these efforts. And we want to especially work towards the mission of serving our member consumers with the lowest possible costs.

And so the test for us is pretty simple. If the RTO can provide lower costs then the coops need to be a

player.

We certainly applaud the direction that WestConnect is taking and especially as reported by Charlie Reinhold this morning to you.

The coops have in the past and we will continue to support the development of an RTO based on six very important principles to us. First, that it takes place in a regional approach.

Secondly, that it includes participant funding of a new facility.

Third, that it maintains critical provisions that are required for those non-FERC jurisdictional systems. And for us that means paying attention to our requirements under the IRS tax rules for our 85/15 requirements, meaning that 85 percent of our revenues come from our members.

Secondly, our ability to reserve transmission to serve our member all requirements contracts.

Thirdly, the ability to recall our available transmission capacity to cover our member all requirements contracts as our members experience growth within their systems.

The fourth principle is the ability to determine our own transmission revenue requirements.

Fifth, the right for us to plan and build facilities and have the first right of refusal in doing

that.

And, sixth, we certainly support the phased approach for RTO development. To implement only those wholesale market elements that add value for the user of the system. To defer the low benefit activity and the high-cost activity and to create organizations and to higher staff and acquire hardware and software only when it's necessary. In other words, do the right thing at the right time and for the right reason.

The coops support and are participating in the WestConnect cost/benefit analysis because we think our consumers will expect to have benefits that are at least equal to the costs of these new facilities and provisions.

We're very concerned that absent a postage stamp transmission rate, as Steve referred to, the small rural consumer and the communities where they are serving or living will be even more disadvantaged as compared to the large and urban customers.

We already experience higher prices in most of our service areas because of the low density nature of our service territory.

You know, we are very much a part of a significant debate, policy debate in this country that's gone on for several years. And I think sometimes for those of us who attend these meetings, sometimes ad nauseam, we forget that

we are really part of this very large debate in this country about whether or not the electricity market should be market-based or whether or not it should be based on meeting the reliable service at the lowest possible cost.

For electric cooperatives we have to remember back to why we were originally created. And the reason we were created was because the marketplace would not serve much of rural America. We think that in many cases today that might still be the case, that the rural consumer, the small customer could indeed be disadvantaged in a pure market-based system.

And so we try to hold these six principles that I mentioned to you up as we evaluate what is going on in the industry today.

Thank you.

MR. GLASER: Thanks, Tom.

There's been some discussion about how involved and how long the restructuring effort has taken. And I think that our next speaker can testify to that. Actually, it's made its way into his title.

Ron is regulatory and restructuring project manager at Western Area Power Administration. You know when it's in your title it's your job.

MR. MOULTON: That's right.

MR. GLASER: Ron's been with WAPA and he's

responsible, as I said, for restructuring and deregulation activities in the electric wholesale power industry. Over the past 15 years he's held a variety of positions at WAPA including transmission planning, resource planning, power marketing and environmental planning issues.

Before joining WAPA Ron held positions at LADWP working in system design, operations, engineering and power supply. Ron holds a Bachelor of Science degree in electrical engineering and a Master's in business administration from the University of Utah.

Our final panelist, Ron Moulton.

STATEMENT OF RONALD MOULTON, MANAGER, ELECTRIC POWER RESTRUCTURING, WESTERN AREA POWER ADMINISTRATION, DESERT SOUTHWEST REGIONAL OFFICE

MR. MOULTON: I think I'm going to stick down here so I can read my notes here.

Chairman Wood, Commissioners Massey and Brownell, Chairman Spitzer, Chairwoman Lovejoy -- I don't know if she's here -- distinguished panelists and guests; Western Area Power Administration appreciates the opportunity to be here today, to participate in this FERC Technical Conference addressing the important issues that relate to the development of wholesale power markets here in the Western Interconnection. Key among these issues we believe is the need for flexibility in both market design and

implementation time frame to accommodate the diverse interest and needs found here in the West. I would like to share with you Western's perspective on this and other issues and hope to develop a deeper understanding of your views and the thinking of others during today's proceedings.

Let me start by providing you with some background information on Western Area Power Administration to help you understand Western's perspective on the important issues that relate to the development of wholesale power markets here in the Western Interconnection.

Western is a federal power marketing agency within the United States Department of Energy. We have been and continue to be active in a variety of efforts to enhance open, competitive and reliable electricity markets. Using more than 17,000 miles of high voltage transmission lines, Western markets and delivers approximately 10,000 megawatts and 41 billion kilowatt-hours of reliable, cost-based energy annually to more than 650 wholesale preference power customers, including municipalities, rural electric cooperatives, irrigation and electric districts, state and federal agencies and Native American tribes in a service area covering approximately 1.3 million square miles in 15 states.

Western's rates for power, ancillary services, and transmission services recover our costs on a project-by-

project basis. Western markets the power generated from power plants at dams constructed and owned and operated by the federal generating agencies including the Department of Interior's Bureau of Reclamation, the Army Corps of Engineers and the International Boundary and Water Commission.

The generation of federal hydro power is by law incidental to certain other project purposes such as irrigation, flood control and navigation. Federal power is sold first to meet the congressionally authorized needs of a project, principally irrigation pumping load, often referred to as "project use" power. The remaining firm power is sold to Western's firm electric service customers. And power available in excess of Western's firm obligations is sold as non-firm to various market participants.

Western strongly supports open access to transmission and has made transmission service available in excess of its existing firm transmission obligations on a first-come, first-served basis since its creation in 1977. Western has successfully participated in coordinated and joint regional transmission planning for many years and has voluntarily filed with the Commission an Open Access Transmission Service Tariff and Standards of Conduct consistent with Orders 888 and 889.

Western supports the voluntary development of RTOs

and is actively involved in discussions surrounding the formation of several RTOs, RTEs and other transmission entities throughout Western's service territory. These includes MISO, Crescent Moon, RTO West, the California ISO, WestConnect RTO, the Public Power Initiative of the West and, most recently, the westTTrans Common OASIS effort mentioned earlier by Mr. Reinhold and Mr. Wiggs in their presentations.

Western is working to assure that the tariffs and market designs of these RTOs meet our unique needs as a federal agency to that we are not precluded from participating in an RTO should we determine the costs to the federal power program of joining an RTO are offset by the commensurate benefits.

Western and the federal generating agencies are stewards of multipurpose water and power projects and have certain statutory and contractual obligations that must be met to ensure that we can commit -- before we can commit to full RTO membership. Some of the key assurances and prerequisites to joining an RTO include:

Preservation of existing transmission rights so that we may continue to carry out our mission of serving our customers with reliable, cost-based preference power;

Preservation of and ability to honor existing contracts and obligations, both explicit and implicit;

Preservation of Western's "final reviewing authority" over operations of the federal transmission assets so as not to improperly delegate our statutory authority;

Establishment of rate designs and transmission pricing mechanisms that mitigate problematic cost shifts to Western due to the large percentage of our customers' load that is ultimately served from a third party's transmission system;

And assurance that any increased costs associated with participation in an RTO will be offset by operational and economic benefits to Western and its customers.

As I mentioned earlier, Western has participated in various RTO formation discussions and has suggested tariff language to address our unique issues and accommodate our unique needs should we choose to partake in an RTO. The flexibility Western needs and has received from transmission owners and other market participants and the progress we've made to date in addressing all of these issues has been encouraging.

Western urges the Commission to provide flexibility in both market design and implementation time frame to accommodate the diverse interest and needs found here in the Western Interconnection in meeting the requirements of a final rule. The Western Interconnection needs the

flexibility to cooperatively identify with the Commission the nature and magnitude of undue discrimination that may exist in the West and the flexibility to craft evidence-based, cost-effective and practical solutions that provide non-discriminatory open access transmission service.

Western believes flexibility provided by the Commission will provide the Western Interconnection with the ability to adopt an incremental approach to address undue discrimination, while mitigating the risks and minimizing the potential for unintentional and unforeseen consequences we have all unfortunately become too familiar with in recent years.

In summary, Western believes flexibility is the key ingredient to successfully dealing with any issues of undue discrimination that may exist within the Western Interconnection. The wholesale market platform begins to introduce the kind of flexibility needed, providing an opportunity to incrementally build upon the present open access practices by implementing wholesale market elements when cost justified and providing for broad and hopefully voluntary participation, both jurisdictional and non-jurisdictional, in the development of wholesale power markets here in the Western Interconnection.

Thanks for the opportunity to share with you Western's views today. And I look forward to your questions

and comments.

MR. GLASER: Thanks, Ron.

Anybody have any questions for the panel?

MR. PERLMAN: My name is Dave Perlman from the FERC staff. Question for Mr. Areghini.

You mentioned something about the SSG-WI process needing adult supervision. And I take it from that that you'd like to see the process move a little quicker or have some more definitive work product and implementation. Please confirm that I understood you correctly. And I'd be interested in other people's views on this panel with respect to the SSG-WI process.

MR. AREGHINI: All of the above I guess I would answer. My observation is that it is, like many ad hoc groups, it is representative of the three RTOs or one ISO and two proposed RTOs addressing seams issues. It would appear to me that it is an ad hoc group, it has had at least one meeting with the WECC Board, and it would appear that it would move along, could incorporate both the market aspect and the reliability considerations if it was steered by the WECC as opposed to its ad hoc formation as exists today.

MR. PERLMAN: Anyone else?

MR. MOULTON: Okay, I guess from Western's perspective I think, you know, we like SRP belong to, as to many other market participants in the West, to WECC and fund

that effort. It's unfortunate that that structure and that organization can't be used more effectively to deal with some of these issues. But we understand that, you know, WECC may be precluded from dealing with some of the issues such as regional transmission planning.

I guess depending on how far RTOs ultimately form here in the west perhaps SSG-WI needs to reinvent itself to include others beyond just the core RTOs, that is perhaps other market participants need to be a part of the steering committee, transmission owners, control area operators, and other market participants until we actually do form RTOs here in the west. And at that point then perhaps it would make sense for SSG-WI to be, you know, structured primarily by participants from the various RTOs.

MR. MCGUCKIN: Tom McGuckin. I'm with the New Mexico State University.

I have a question about when we talk about the formation of RTOs and particularly about WestConnect and its direction at this point, having been a graduate of DesertSTAR and watched the evolution to WestConnect I'm sort of curious right now what the roadmap is for WestConnect going forward, and particularly WestConnect vis-a-vis other participants, not the TOs but the let's say the other stakeholders involved? Because we all went through this song and dance about a year-and-a-half ago and things were

changed on us. And now they appear to be changing again.

So if you could address that, where we're going here as far as stakeholder involvement in the future of the RTO here I would appreciate it?

MR. MOULTON: Charlie?

MR. REINHOLD: Let me grab this one.

Tom, WestConnect during the pendency of its order at FERC has certainly had less of a stakeholder process involved. WestConnect did though have a stakeholder meeting last week. We had relatively light attendance but we did outline just exactly what you were asking, where WestConnect was, where it's headed. Certainly that was a big part of my presentation this morning.

So rather than repeating that I would say I'd be happy to visit with you about what the specifics are and some of the timelines we're looking at. But we are looking to moving forward with our cost/benefit analysis, certainly implementation of the RTO functionality as it makes sense immediately with the westTTrans and OASIS, Common OASIS system for much of the Western Interconnection and on to other pieces of RTO functionality as they work in and as we can get them implemented.

MR. BANDERA: I'm Derek Bandera with the FERC staff. I think this is going to go back to Charlie on WestConnect.

It seems to me from my interpretation of the WestConnect filing that was submitted and for the most part approved in its entirety by FERC except for a few minor items that you've listed, okay, my question is why after it being accepted now you decide that there needs to be delay for a cost/benefit study after basically what was voluntarily proposed was accepted, and now there seems to be a step back and cost/benefit study to what people agreed to seems to be in a voluntary stakeholder basis? It just seems odd to me. If you could explain sort of how that came about?

MR. REINHOLD: Sure. A couple of things happened. First of all DOE issued a study which said there were minimal, if any, benefits in this region of this country for RTO formation. That certainly raised a bit of a red flag.

The other piece is the cost/benefit analysis is needed for the local regulatory processes, whether it's the state commissions for the self-regulating entities that are participating, the coops, the municipals. All of them have to justify before their regulators why they should move forward with WestConnect.

So the cost/benefit analysis was always thought to be necessary at some point. Now is the time when we're putting it together.

MR. BANDERA: Well, shouldn't the cost/benefit be

done before the filing and when you were putting it all together in the first place? It would seem to me that would make more sense.

MR. REINHOLD: It may have made some sense at the time but it's certainly necessary now in order to get the final approvals for the TOs to transfer operational authority of their assets to this operating entity.

COMMISSIONER BROWNELL: In the development of the cost/benefit analysis during the less than developed stakeholder process will you include stakeholders and other market participants to be sure that you're getting that fully developed study that I asked about before? And will you ask questions about economic development and environmental benefits or will you do it strictly on a per kilowatt hour or some kind of basis on that? Have you thought that through? Thanks.

MR. REINHOLD: I haven't, we haven't thought through I don't think all of the detail towards the end of your comment.

We did have an open process. We had several stakeholder meetings. We had public sessions. We put it out on our blaster notice on our website. We did have a tremendous amount of interest as we were getting into the stakeholder process.

And as we started through we certainly wanted the

folks who were funding that cost/benefit analysis to have full participation. And we did have that full participation by at least the 16 entities and probably even more entities than that who ultimately decided not to contribute funding to it.

So we have opened it up. We've noticed it. We've had participation. A lot of interest from vendors. We learned a lot from the vendors. Your suggestion on environmental features and economic development I think is something that we certainly need to make sure we look at and capture if it's relevant to the study.

MR. THOMAS: Hi. Chris Thomas with the FERC staff as well.

I want to change a little direction because clearly it's important of the non-profit, coops and so forth in the Southwest to participate in this endeavor. And something that maybe I'm a little confused about or haven't heard the full story, and maybe you can take it up to explain this a little bit more, this notion of the right still to know over others. I'm not sure that we've heard the full story of why that's so important or why you wouldn't get the benefits if someone else proposed the project, that you have to own it to make sure you get some sort of benefit out of the RTO?

MR. FAUSETT: Well, I think you have to realize that many of us, I'll speak for Tri-State only, but we

believe in the philosophy that we offer least cost power to our members and our consumers. We were very disturbed with the initial SMD design because it treated transmission rights in a financial sense, we believed we were threatened by the fact that we severed our very low cost coal plants, which are remote plants, from our load centers which are along the front range of Colorado and in New Mexico.

We have been exposed to the markets during the price run-ups and other places and we've come down firmly on the side that we want to control our own destiny through a vertically integrated structure, including the purchase or the construction of transmission necessary to move generation to loads. We don't believe that the substitution of financial rights in the form of LMP or auctions or anything else that's been proposed along the way will give us the surety that we need to move low cost resources to our load centers.

We're not heavily into the market in the sales. We're not, we're building for our own requirements not for speculative ventures in the market. And we'd like to stay that way. And I don't see any reason an RTO can't be formed that would recognize those needs from those of us in the public sector.

MR. JONES: I don't think I could add much to that except that I think it's one point that gives us another

filter in making a decision about whether or not to build facilities.

MR. GLASER: The other two declined.

CHAIRMAN WOOD: Steve, you mentioned something about postage stamp, you mentioned a closing shot on postage stamp. And, Tom, in your litany I think item number two is --

MR. JONES: Postage stamp, yes.

CHAIRMAN WOOD: Well you said participant funding. So I just wanted to see, you want it or you don't want it?

MR. JONES: We certainly recognize the importance of participant funding, especially in Arizona here where we have a number of merchant plans that are going in ostensibly for serving the California market. And we feel like that in the unique nature of these new plants in Arizona that really participant funding is probably very applicable to Arizona.

Nationally we think our national association, for example, does not have that same strong feeling about participant funding, the National Rural Electric Cooperative Association. But we realize this is a regional difference where we might be different from our national association because of the nature of the new plants that are going in here and where power is likely to wind up that participant funding is important for Arizona.

We would have a hard time in the area that we

serve, the consumers that we serve in Arizona justifying to them additional costs for transmission on the grid that was done primarily to serve a California load.

MS. SIMLER: Jaime Simler with FERC staff.

Building on your question or your comment on participant funding and what I thought I heard Mr. Areghini talk about with the CATS, with the Central Arizona Transmission System, for the participant funding for, if it were to go through for generators in Arizona, and assuming then, you know, impacts on third party systems, what is the mechanism in place now to deal with getting the transmission built not only through participant funding within Arizona but making sure it syncs up with, for example, any infrastructure needed in California? I'm just trying to understand what the current state of affairs is for making sure that that all lines up.

MR. AREGHINI: I'll take a shot at that.

With respect to the reliability impact that is all done through the studies that are made prior, under the WECC prior to the project being undertaken.

With respect to the adequacy if you will, it is strictly up to the participants to determine the size, shape, direction, beginning and ending point of the transmission addition. You know, they are financing it. For example, let's assume we have a project now where there

are four owners. Those four owners make the determination where the beginning will be, where the ending will be, what the capacity will be. Then that is studied relative to the impact of the system reliabilitywise. Assuming that there are no detrimental effects then it is constructed.

We do not, you know -- the opportunities are there, for example, if you were building something in Arizona and somebody wanted to piggyback on it to add a line to California those opportunities are there because it is very much noticed in the planning processes. So it's up to some other entity to if they feel so desire to step forward and add to that process.

MR. JONES: We have a specific example of that here where on a voluntary basis we worked with Caltine to do improvements to facilities up in the northwestern part of the state and to southwest transmission cooperative facilities to make improvements necessary for them to get the power from their new plant to the places where they want to serve, mostly in California.

COMMISSIONER MASSEY: Ron Moulton, when you were speaking you mentioned in passing that undue discrimination may exist in the marketplace. I think I heard those words.

MR. MOULTON: I think what I was trying to address is that before we leap to some conclusions about what kinds of wholesale market elements we need here in the West that

perhaps we ought to spend some time identifying what undue discrimination exists in the West and create a cost-effective, fact-based, you know, solution to that problem, whatever that problem may be.

COMMISSIONER MASSEY: Well, I wanted to ask the members of the panel whether, I think one of the key rationales for the RTO is to ensure the independent operation of the grid to ensure that there is no discrimination in providing access and that all generators have a level playing field, and that there is, not only does the playing field exist but there is the perception, there's high level of confidence that a level playing field exists. And based upon my travels and my understanding of what's going on literally all over the world every country that is trying to move to a market-based approach is struggling with that issue and wanting to ensure the independent operation of the grid, independent of merchant interests. It's not just FERC's sort of wacky idea.

And I wonder what those of you on the panel think about that as an ultimate goal for the West and for the Southwest? Do you think it's necessary in the Southwest or do you think it's simply an environment where there is absolutely no discrimination and no possibility of discrimination in providing access to the grid?

It's a central issue it seems to me. And I'm just

playing devil's advocate here. Based upon the presentations of members of the panel it sounds like everybody thinks things are just fine the way they are right now.

And I wonder if anybody questions that?

MR. WHEELER: I'll start but I'd also like to see if we could get Steve Glaser to say something substantive today.

(Laughter.)

MR. WHEELER: I will start by saying part of my earlier remarks were dedicated to the question of is the factual predicate there for having to go as far as having all of the particular elements of SMD and RTO that FERC in its grand design would envision. And my point was simply let's make sure we understand what specific problem we're trying to solve. And if your question is could there ever be a situation in which there was undue discrimination? Of course. The question is what's the remedy for a perception?

And our point is that you ought to take it in steps where you can get the buy-in from all the necessary parties, steps that show that the costs of taking the steps will produce real value.

In terms of what's the track record, I think just by looking at the amount of generator construction and generation interconnection that has occurred in Arizona at the merchant level there's both been utility generation and

merchant generation. And we've done a number of things that I think have facilitated merchant interconnection.

We were the first ones in the Southwest to have a pro forma generation interconnection tariff. With SRP's help and other help there is a very innovative common bus situation set up at Palo Verde to expand the interconnection opportunities there without having to pay additional wheel-in charges. APS has sited and built lines that have helped interconnection for generating plants.

So I think if you look at the track record you'll see that there has been a lot of cooperation between the transmission owners and the merchant generators themselves to help facilitate their connection to the grid. I'm sure it hasn't gone completely perfectly to their point of view and there are probably improvements we can make. But the question is at what price? And do you really have such a poor track record that you have to make a drastic change in the way you're doing business now?

And that was simply the point I was trying to make.

MR. AREGHINI: I'll just add to that, Commissioner Massey, I believe that discrimination in some people's eyes will exist until people who don't own the transmission have as equal access to it as someone who does.

For example, if we have a right from say the Navajo Plant to the Phoenix area on a transmission that we own I am

sure that there is an element out there that will say that's discrimination. We don't believe so. I believe the issue is who has rights and who has access and who has knowledge of transmission that is available that is not allocated to one of the owners. And that's where this Common OASIS will be extremely helpful.

Right now the biggest, one of the biggest complaints we get from merchant operators is I've got utility A and I've got utility B and I've got utility C, you all post transmission differently, you rate it differently. This Common OASIS should take care of that.

But I don't think that the -- and we're fully aware that there is always this issue of discrimination that in some people's eyes it will always exist until the conditions exist that I described before.

MR. GLASER: Well, Steve goaded me into it.

I want to take the CAT Study for an example. And this isn't an absolute, but we do open up the process for transmission planning in the state to all participants. And I think everybody would agree that it's not, as David said before, unfortunately when push comes to shove and it's time to do the study work and pay for the study work really what you're looking at is us paying, him paying and the guy at the end paying and there's a lot of free ridership there. And we're trying to make a more conducive way to plan in the

state.

But, you know, when everybody participates up to a point and then says, well, we can't go any further, that puts a chill on the whole planning process. And I'm not sure exactly how an RTO will accommodate that when the funding of the RTO in and of itself is going to have those same issues.

MR. HATCH-MILLER: Jeff Hatch-Miller, Arizona Corporation Commission.

I'm going to try to ask this question maybe from another direction. Is there a way without threatening your ability to provide for native load that a line or lines could be built to move, and it sounds like one of the goals of FERC, to move electricity from our region into California could be built that would be open to all comers in some way separate than the system that might impact your native load?

MR. WHEELER: Short answer is absolutely, yes. Somebody just has to decide to want to build one, finance it, site it, get the requisite ownership structure in place and the people who want to use it. And that is not foreclosed to anybody with the ability and willingness to do that.

So the short answer is yes. And to the extent that you are seeing some perceived congestion issues or other strain on the system issues you have to recall that

virtually all of the new generation, particularly the merchant generation, was not accompanied by increases in the transmission capability. The investments that, for example, our company is making and I presume SRP and TEP and the others here, are primarily directed toward native load because we know there is a specific need and a specific location. That's where our 800 million of new transmission investment is being directed.

That doesn't mean we wouldn't participate in other projects but it also means that no other participants are foreclosed from proposing their own projects if they can see a need to develop a project in a different area at a different place.

COMMISSIONER BROWNELL: Could I try and answer the Commissioner's question in a different way because I think the issue of native load comes up everywhere, and of course we're all interested in protecting native load, and I'm unaware other than California where of course there weren't markets and there was an insufficient commodity and there were the wrong incentives and there was an insufficient delivery system, I am unaware in any other developed market where native load was harmed. So I think in answer to your question when you have independent grid operators who in fact do the studies that market participants fund in a way that the TOs do not they're a disproportionate part of the

burden. But they are assured all participants as they are paying the bill that the studies that they're getting are independent and have no dog in the hunt, I think that's the value added.

But I'm unaware of any other market, and maybe, Pat, you want to speak of ERCOT, where native load was actually damaged.

So clearly there is a way, Commissioner, that you can manage the system and manage the investment and allocate costs where native loads are not harmed in terms of reliability or costs.

But, Pat, maybe you also want to.

MR. TOTTEN: I don't think it was a significant issue in ERCOT. And I don't really see it as a reliability issue, and maybe I'm missing the boat. It seems to me that you're primarily talking about economic issues. And I see it in the context like New England, for example, where they change the way they operate their system and the result is that you get higher costs in the parts of New England where the transmission system is constrained. And I guess I see that possibility in any system but I really don't see it as a reliability issue.

And I should say I'm Jess Totten and I'm with the Texas Public Utility Commission.

CHAIRMAN WOOD: I want to thank this panel very

nuch. And we will slide swiftly to the final panel which will be the non-TO market participants here in the Southwest.

(Brief recess.)

CHAIRMAN WOOD: Okay, if everybody could go ahead and take a seat.

(Pause.)

CHAIRMAN WOOD: Before we start this last panel I want to -- let's go ahead and grab a seat, please.

Thank you, Commissioner.

Before we go to this last panel I want to take this brief opportunity to recognize the members on our agency staff who do the day to day work with our Western Region. And if they could just stand up while I recognize here. And I also have a little sheet here with names and phone numbers. So for those of you in the market that want to know and what to have some follow-up contacts at the FERC other than the three of us who are here on the Commission I want you to please take advantage of that opportunity.

Jaime Simler is here, Derek Bandera, David Perlman and Chris Thomas who are all on our market side. David is one of our lawyers here but we like him anyway.

We also have Sarah McKinley who as you know has been coordinating all this.

From my office Rob Gramlich. And from Commissioner

Massey's office Bud Earley.

And I think that should be all of us. Great?

Our last panel is going to be moderated by Michael Grant. So with no further ado.

OPENING STATEMENT OF MICHAEL M. GRANT, GALLAGHER &
KENNEDY

MR. GRANT: Thank you very much.

Good afternoon. You know, a quick story on Tom Jones who was up for Grand Canyon the last panel discussion. He really carries this singer thing way too far. If you call his cellphone and he doesn't answer and it goes to his voicemail his message says "This is Tom Jones. It's not unusual that I can't answer your call."

(Laughter.)

I think Tom left.

Very good to be with you this afternoon. And for our distinguished guests from Washington we thought you might be suffering from HWS, that is hurricane withdrawal syndrome, so we ordered up a little tropical depression for you this afternoon in Phoenix.

The FERC as part of their technical conference wanted views on WestConnect and westTTrans from other stakeholders. I suspect this is where we will get Commissioner Spitzer's healthy tension in this discussion. And to that end we have assembled interests ranging from

generators to alternative energy providers to residential consumer representatives.

Unlike Steve I didn't have the foresight to ask any of these people for resumes. There is a disadvantage to that. The disadvantage is you will have absolutely no idea who these people are. The advantage is the introductions will go like lightning.

So without further ado let me turn this microphone over to Steve Huhman. He is director, market design and regulatory affairs, West Region, for Mirant.

STATEMENT OF STEVE HUHMAN, DIRECTOR, MARKET DESIGN & REGULATORY AFFAIRS, WEST REGION, MIRANT INC.

MR. HUHMAN: Thanks, Mike, I appreciate that.

I want to start off just to note that when I first walked in I thought perhaps I was miscast on the wrong panel given that the name Steve was pretty popular on the first one. But I notice we've got three Steve's on this panel too, so we're going toe to toe with them in the Steve category.

When I thought about what I was going to say today rather than just sort of say the same old things that you've heard generators say for a long time I thought I'd step back a little bit and try to get a little retrospective perspective on the vision we've had to open access transmission over the past several years.

Remember when we all thought that we were going to use our experience from the gas industry restructuring to totally restructure the electric industry in three years? Anybody remember that? A few. Okay.?

Turned out to be a little more complicated than that apparently. But I thought a little bit about the vision and where we've gone over time. And I think our initial vision was fairly simple, we simply wanted open access transmission so that all generators could access all potential customers and they could engage in willing transactions and that the market would be much better off and there would be tremendous amounts of benefits to all consumers from simply making sure that all willing buyers and all willing sellers were able to access each other.

And that was phase one of the vision which for shorthand I'll call the OAT vision, the Open Access Tariff.

As we started working along that line people started thinking about this a little more and I think people got more excited about the prospects and the visions broadened and expanded and we went into phase two of the vision which I'll call the RTO vision. And at that point in time we thought that rather than just simply have open access by an integrated utility what we really needed was a broad-based kind of an entity that would combine and integrate control areas, that would operate individual

markets, that would be a provider of last resort for energy and ancillary services and would provide a much broader range of access and services and we hoped, obviously from a public policy perspective, provide an even greater range of benefits to the ultimate consumers because that is after all what this whole exercise is about.

Phase three of the vision which is where we are now with yet a further expansion, I would call it for shorthand the quasi-governmental organization, we're not thinking in terms of using an RTO or an ISO as an entity that not only will provide all those services but also will create, organize and administer markets and exchanges as well as just the transmission system, that will have some quasi-governmental powers in terms of market monitoring and perhaps punishing and penalizing inappropriate behavior. And so the vision really continues to expand every time we rethink it.

And I'll just say that as a contrast I look at the DesertSTAR/WestConnect activity that's gone on over the past several years, and no disparagement at all to the people involved because I firmly believe that the people involved have been acting in good faith, but really if you look at where we were with DesertSTAR potentially about 2000 or 2001 the vision for DesertSTAR actually seems to be contracting rather than expanding.

And so our only observation is from a generator's perspective is that in the Southwest, and I do understand the wide range of issues that cause people to want to pull back a little bit on their vision of a DesertSTAR or WestConnect, and I also acknowledge that a lot of those issues are very legitimate, but we seem to be contracting in our vision in the Southwest rather than expanding in our vision. And so I hope that as we continue to work through this process we have that sense of perspective and take that step back and start thinking about how can we expand the vision of WestConnect and the former DesertSTAR in the Southwest and other sorts of things and get back kind of in sync with where the vision for the rest of the country is going which is an expansive vision, an improved vision, do more things and provide more consumer benefits ultimately.

As far as the new joint OASIS activity is concerned don't know a lot about it yet. Just heard about it within the last couple of weeks. Haven't seen a lot of details about precisely how it's going to work. So I will give you an initial impression or initial reaction to it.

I think taken in isolation it's a very positive step. I know one of the very important factors that a company like ours is hoping to get out of this whole process was some standardization in terms of both information systems and tariff rules in order to help is drove costs out

of the system. And a company like ours that operates in multiple venues has to have a separate interface system for every RTO or ISO or anything of that nature that's out there then clearly having several of those combined into one will help us drive some costs out of the system and it will have to be an improvement in efficiency for companies like ours.

That having said, there is a couple of quick questions that pop to mind. I don't know to what extent the new combined OASIS will have standardized rules, for example, in terms of posting available transmission, or will the end agent owning that transmission continue to do their own ATC calculation using separate methodologies?

Do they agree to post all of their available transmission, however calculated, on the OASIS at all times or will they make decisions at different times what to post as available and what to withhold?

These are open questions that would impact the ultimate reaction to the common OASIS.

And I guess the final comment I would make is that while we welcome it very strongly and think it's a great interim step perhaps we just are a little bit concerned and want to make sure that it doesn't end up being an excuse for going more slowly in the broader process of moving to a full RTO in the Southwest simply because you've already got something in place that meets some of the needs.

Thank you.

MR. GRANT: Thank you very much, Steve.

Scott Gutting of Energy Strategies Company coming up here indicated that he has a plane flight constraint and asked if he could be moved up in the order. And I'm happy to do so. So here's Scott Gutting of Energy Strategies, Incorporated.

STATEMENT OF SCOTT GUTTING, ENERGY STRATEGIES, INC.

MR. GUTTING: Thanks, Michael.

We're representing Arizonans for Electric Choice and Competition which is a group of customers in the state that have a little bit over 1,000 megawatts of load. We have participated in DesertSTAR from the beginning and WestConnect, in fact provided comments on the order which the Commission and staff supported us on. We appreciate that very much.

To just be brief in terms of our comments, we've been involved in this process since 1995. We have been active participants with all three utilities in the state. And we applaud your consideration of regional issues associated with the White Paper that came out in April.

We also supported the WestConnect protocols regarding native load and particularly native load following customers that might leave from the traditional investor-owned utility structure because Arizona is a retail access

state.

And we appreciate you all coming out here. Next time if you want to come to Salt Lake which is my domain we'd be happy to hold a meeting in January or February.

Thank you.

That was less than five minutes.

MR. GRANT: Moving right along. John Woodley is next from Morgan Stanley Capital Group.

John, want this one or you want to work off that?

STATEMENT OF JOHN WOODLEY, MORGAN STANLEY CAPITAL GROUP, INC.

MR. WOODLEY: Actually I'm a little jetlagged so I'm going to stay seated if that's okay with everybody. It's quite a visceral experience. I was in London and the conditions are semi-desert over there and I flew in here last night and it felt like a tropical rain forest.

(Laughter.)

I'm not quite sure where I am.

But I suppose just to give a quick background into Morgan Stanley, Morgan Stanley Capital Group is the licensed power marketer, the subsidiary of Morgan Stanley, the parent. Basically although I suppose you could describe us as a marketer we're a part of a large global, diversified financial services firm. And our product mix reflects that.

And without really going into the product mix much,

unless you want to ask me about it later in question and answer time, we put capital to work in this industry. And I thought that for the theme of my talk you're probably most interested in what makes a company like ours and Wall Street in general put capital to work here versus somewhere else?

We do in fact compete for use of the balance sheet. And we compete against all kinds of markets around the world. So one of the things that I thought I would allude to that happened this morning, I think it was -- it probably wasn't put quite this bluntly but I think Wall Street was suggested to be a little fickle. I would agree with that. Investors can lose interest extremely quickly. They're very risk averse. And if they don't understand something they tend to move on to something that they do.

So I would actually completely agree with what was said this morning. I don't think there is a general view in Wall Street that the only workable model is a vertically integrated, cost of service, regulated utility. I don't believe that at all. In fact, in our part of the shop I think we believe that vertical disaggregation is in fact the norm in an industry that moves into competition.

Horizontal aggregation might also be the norm which is something else to think about. But vertical disaggregation is what we see and in fact facilitates the role that we play. We buy what people want to sell and we

sell what people want to buy. And you've got to put a lot of money behind that obligation for people to trust that contract. That's the capital we've got to put at work.

Now, buyers and sellers you would think, well, gee why don't they just go directly to each other? Well, the answer is they want fundamentally different products. Someone who is trying to build and finance a power plant wants a long-term contract, they want fixed payments every month, and they want fuel price pass-through.

What's the first thing that goes out of the window when you deregulate retail electric markets? The fuel cost recovery clause. That's the last thing that retail customers want. They also tend to want a fixed bill every month but they tend to want shorter term contracts.

So we provide these contracts and we provide them most effectively, and there is no coincidence to this, most effectively in the Northeast. Those markets are relatively nature and they work relatively well. We're very, very pleased with the infrastructure there and we're a participant in almost all aspects of that, including I think a controversial point here, the financially settled transmission congestion contracts.

We have no particular program with the way those markets have been put together and the way they're operated. It's a place that we can bring capital to work. We get

approval to do that very easily.

One of the things that I think that you are going to have to think about in the process here of course is that if you create your own thing if it's too new, too different, too little understood you're going to have to spend a lot of time convincing investors to put capital to work here, something that really needs to be thought about.

A competent economist I'm not -- by the way I didn't say I'm neither, I said I'm not -- could give you all the elements of an efficient market. I'm just going to focus on a few things that I think may be worthwhile thinking about. The things that we are most concerned about when we monitor what's going on in markets like this is do we have regulatory clarity and consistency? That's very, very important for us. It's something we can't hedge and it's an awful risk to take. I know, I spent most of my time in Washington last year.

The second thing is I would suggest that you need to be thinking geographically large and no seams, consistent across a wide area.

The other thing is, always comes up in our conversations, contract sanctity. That's a very important piece of any economy, no matter what you're talking about.

And the final point which I think people have alluded to is equal access, in other words no incumbency.

Just as an example to that I would point out that if you, for example, link the requirement that somebody physically flow power across a transmission congestion contract that is a disadvantage to use, an advantage to someone else. That doesn't make a level playing field.

One of the things I want to finish up with is just to point out if you will notice that I didn't mention in here was simplicity. Simplicity is not a requirement. I know that's going to sound counterintuitive. But the reason I'm going to say that, I think that well-intentioned attempted to create simplicity can have the opposite effect of what you want.

I'll give a simple example there. In the incarnation of the market that we think would work we would expect LMP to exist, nodal spot pricing. If you try to simply in the initial incarnation by going to flow gates or zonal prices we cannot offer long-term contracts in that environment because we know it's going to change. So you'd be better off I think going straight to the more complex structure. I know that's controversial but I offer it for what it's worth.

Anyway, with that I think I'll leave any other comments you may want to hear from me to your questions.

MR. GRANT: Thank you very much, John.

Dennis Delaney is also here today. He is from K.R.

Saline & Associates. And he is speaking for the Arizona Consumer Owned Electric System.

Dennis, take it away.

STATEMENT OF DENNIS L. DELANEY, K.R. SALINE & ASSOCIATES, PLC, FOR ARIZONA CONSUMER OWNED ELECTRIC SYSTEMS

MR. DELANEY: Thank you, Mike.

My name is Dennis Delaney and I am here today on behalf of the Arizona Consumer Owned Electric Systems. And behalf of the ACES members I'd like to thank Chairman Wood and the other FERC Commissioners for allowing us to participate in today's technical conference.

The ACES members are small utilities, political subdivisions and special districts which comprise the vast majority of the public power transmission dependent utilities in Arizona. ACES has been active in the proceedings before the Commission involving wholesale and transmission aspects of electric power industry restructuring in Arizona and in the Western Interconnection.

ACES participated as a group in the efforts to form an RTO in the Southwest for many years, beginning with the development of the non-profit DesertSTAR. In early October 2001 the transmission providers abandoned DesertSTAR in favor of the for-profit WestConnect structure.

While ACES remains unsupportive of the WestConnect for-profit structure, ACES is participating in the

WestConnect cost/benefit analysis and we support the phased-in approach outlined earlier by the WestConnect sponsors.

ACES also welcomes and supports the westTTrans proposal and applauds the transmission owners for their efforts in developing a single OASIS. We are particularly encouraged by the focus of user tools and the development of a secondary market for transmission rights. We will reserve our comments on the energy products or the energy products bulletin board at this time but believe, given time, the bulletin board will provide opportunities for enhanced wholesale energy markets in the Southwest.

The WestConnect phased approach is consistent with the ACES SMD Comments to "walk before we run." The phased approach provides time to ensure and demonstrate that changes in the industry's structure will indeed provide the intended benefits. Of great concern to the ACES members is the rush towards an LMP market that has not yet been demonstrated to provide benefits to the ultimate consumers.

FERC should ensure that prior to the implementation of an LMP market, consumers are afforded an opportunity to fully understand the complexities and the significant risks associated with LMP markets. Implementation of LMP markets must be accompanied by appropriate safeguards including full disclosure of the impacts and opportunities for a detailed review of the modeling assumptions.

FERC must also ensure that the market participants are afforded opportunities to a meaningful dispute resolution process to fully vent disagreements prior to LMP implementation.

Attached to these remarks are an extract from the ACES Comments on the SMD NOPR. And the attachment spells out some specific safeguards that the Commission should insist on before any LMP market is implemented in the Western Interconnection.

Of utmost concern to the ACES members is the allocation of congestion rights. Without careful implementation unintended consequences may very well result in unmanageable risks. At a minimum, the allocation of congestion rights should ensure that the service we have going forward in an LMP market is equivalent to the service we have today.

Another concern the ACES members have is the identification and mitigation of market power and market abuse. The smaller transmission dependent utilities have little choice but to assume that the market monitors will be empowered to swiftly identify and stop market abuses long before market meltdowns occur. ACES supports a fully transparent process which errs on the side of the consumers versus providers.

Again, I would like to thank you for the

opportunity to provide these comments and would be happy to try to address any questions you may have.

MR. GRANT: Thank you, Dennis.

Chris Ellison is here from the American Wind Energy Association.

Chris.

STATEMENT OF CHRIS ELLISON, AMERICAN WIND ENERGY ASSOCIATION

MR. ELLISON: Thank you, Michael.

My comments today are on behalf of the American Wind Energy Association but I'm speaking for myself based upon my experience not only for that association but for other similar clients throughout the West.

I want to begin first by joining everyone else in thanking Chairman Wood and his fellow Commissioners and staff for making this trip out here and for providing this forum. Thank you very much for doing it. I think it's been a very constructive day.

I also want to second Chairman Spitzer's comment this morning about the importance of having a constructive dialogue between particularly the state commissions and the FERC and to agree wholeheartedly with him that the kind of dialogue that has occurred specifically in California has not been constructive. I think today has been constructive and I come away from today discouraged about some things but

certainly encouraged by the dialogue.

Transmission access and market design is the single most important thing to the development of wind energy in the United States right now. The association has identified it as the highest priority problem for the continued development of that renewable, clean resource. But what I want to tell you is that the reverse is also true. In my opinion solving the problems that may at first appear to be unique to wind energy is also critical to the successful development of markets and transmission policies. And in that sense wind is sort of the canary in the coal mine if you will for whether markets work, not just for that resource but for many others.

And I say that because of the characteristics of wind. For example, wind is typically a new entrant into the marketplace. If you solve the problem of wind you solve the problem for all, remove the barrier to entry for all new entrants.

Wind is intermittent as we all know. If you solve that problem for wind you also solve it for solar but, more importantly, you solve it for demand response which is I think the ultimate way that you want markets to work and to protect consumers from market power.

Wind is also remote and its location constrained. If you solve the problems that are associated with that for

wind you remove pancaking, you create a transmission plan that works for regional transactions for everyone.

So I think wind has a special place in the development of proposals such as WestConnect. And I urge you to focus on those problems not only because of the environmental benefit and the economic benefits, diversity benefits that come with that resource but because of what it represents for the market as a whole.

There are real problems with the status quo. One of the things that I'm discouraged to hear is sort of the discussion implying that here in the Southwest or in the West we don't have the kinds of problems that justify restructuring. I'm going to focus on three or four that are most important to wind.

Clearly lack of independence and undue discrimination is a real problem. And in response to Commissioner Massey's question I think there is a long history, a well-documented history of discrimination by those who operate monopoly transmission systems and also have a financial interest in the market.

And just by way of one example, I know more than that I can point no further than the WestConnect filing last year itself which proposed a distinctly different and easier interconnection process for generation facilities owned by the PTOs and for those owned by others. The FERC rejected

that but it's certainly a very explicit example of the kind of thing that the reason that we need independence.

Pancaking is a real problem and it's a problem in the West, it's a problem in the Southwest. Any solution that we comes up with needs to address that. Particularly important to wind because of its intermittency is the lack of liquid, fairly priced balancing market. Excessive deviation penalties and those kinds of things continue to be a problem in the West. They are a problem in the Southwest. And we need to solve for that.

And although we are making some progress through SSG-WI on transmission planning and AWEA is working quite closely with the SSG-WI planning group on that and is encouraged by that effort, the fact remains the transmission planning is a problem in the West and it is a problem in the Southwest as well. And so we need to solve for that as well.

Let me offer one sidebar comment and then conclude. The sidebar comment is that wind is not looking for a subsidy here. And I think it's often accused of that. Transmission policies have been developed over the years with particular resources in mind. And as new technologies come aboard transmission policies need to evolve to accommodate those technologies.

But, for example, it's considered perfectly

conventional to expect that conventional resources like gas fired facilities and whatnot have ramp rates and that you have to developed transmission policies that accept the fact that they have to ramp at certain rates. Well, the intermittency problem with wind is analogous to that. It's not some subsidy that we're talking about here, it's simply designing policies that work for the kind of generation that you want to have on your system.

With that sidebar comment let me conclude by saying that AWEA has been a strong supporter of standard market design. We support WestConnect if it's fully and timely implemented. We hope that people move forward with that.

And, lastly, let me say to those of you who have concerns with standard market design or concerns with a full implementation of WestConnect that we're certainly open to alternatives. But the status quo from at least our perspective is not acceptable. And I would urge all of you who have problems with standard market design to ask yourselves what's your solution to the problems that I've identified and the problems that we all know exist?

Thank you very much.

MR. GRANT: Thank you, Chris.

We get to the final two Steves on the panel. The first is Steven Begay. He's general manager of the Dine Power Authority which is an enterprise of the Navajo Nation

and also the developer of the Navajo Transmission Project from the Four Corners area over to the marketplace.

Steve, it's good to see you again.

STATEMENT OF STEVEN C. BEGAY, GENERAL MANAGER, DINE
POWER AUTHORITY

MR. BEGAY: Thank you. Good afternoon.

Mike Grant used to be our attorney when we were going through the CEC process and we had three public meetings before the Corporation Commission gave us a CEC for our transmission line. That was a couple years ago.

I have been general manager for Dine Power Authority. It's an enterprise of the Navajo Nation. And I think just real quickly there are about 300,000 members and about 170,000 of those individuals live on the reservation. About 37 percent of the residents do not have electricity even though we're probably the key coal supplier to three big generators in the Four Corners and northern Arizona area: Navajo Generating Plant and the Four Corners Power Plant and the Mojave Plant, that's in Nevada. So coal resources come from northern Arizona and northwest New Mexico for those plants.

We have no megawatts of generation right now. We don't own one inch of transmission line right now. But we're building a 470-mile, 500 kV AC transmission line from the Shiprock Substation through northern Arizona into

southern Nevada to a marketplace substation. I have a handout here. I will Sarah an electronic copy too. And this is basically for the benefit of the Nation. We have a lot of coal resources. We feel that we can build a generation plant.

We tried that in 1985 when DPA was formed. And after five years it was determined not to be feasible at the time and it went to a transmission only NTP project. And it crosses, the NTP crosses several jurisdictions. About 61 percent of it crosses Navajo land, trust land and fee land in the Big Boquias area. It covers forest lands, Park Service lands, recreations lands, BLM lands and some private land, so there's a lot of right-of-way activity that we're working on. And I think the substantial portion is done.

We have a right-of-way from the Navajo Nation Resources Committee. If we want to start construction on the line we can start at the Big Boquias Ranch right now. And with the BIA approval on the federal right-of-way for the trust lands portion we can also start about 285 miles of the 470 miles.

So we're getting close to construction. We have a development partner Transelec. I think Transelec just finished a deal with California on path 15. It's about an 82-mile, \$300 million project. NTP is 470 miles, about a \$600 million project with probably about two-thirds or

three-fourths of that are going to be an EPC contract.

So in terms of dollars per mile we're like five-and-a-half times more cost beneficial than the path 15 line covering EPC's \$400 million, 470 miles of line versus 300 million for an 82-mile line. You can tell that in the long run I think that we will help the consumer in the end.

Now, the line is an interstate line. There are not very many lines that are like that being built today. In fact, this might be the largest line in the U.S. It starts in the WestConnect area and it will end in the RTO West area in Nevada. So we definitely will be involved in the same issues.

We had a call from the step group and our data is in their analysis. So hopefully when the analysis is completed we will be in that study.

We follow the existing lines that we're going to parallel the WAPA line from Shiprock to Page area. Then we follow the hydro lines, the WAPA lines and the Navajo Generating Station power lines to Moenkopi Substation. And we end up in marketplace substation, another 220-plus miles for a total of 470 miles.

And we are not -- we try to keep away from new lands. We follow the parallel path so to minimize the environmental impact.

Now the ROD, what we call the ROD, the record of

decision from the federal Department of Energy stated in there the line, this was back in 1995 or '96 when this was being discussed, relieving the constraints of the transmission of electricity west of Four Corners, that's been identified. And we feel that NTP will help with that. Improving the operational flexibility and reliability of the high, extra high voltage transmission system in the region, allowing for increased economical power transfer of sales in the region -- purchases in the region

We have a Tribal Utility Authority, Navajo Tribal Utility Authority who buys federal power from several federal sources. But if the NTP is built what it will do is it will relieve that 230 line. And if that 230 line is -- if NTUA can buy more power off that line that's a benefit to NTUA without really tying into the NTP. But we have a bay in the Page area where we have a stepping, stepdown facility that will convert the 500 kV to a 69 kV line for NTUA use, that way power from the hydro doesn't have to go all the way down to central Arizona and then back up the APS line into Tuba City. We'll be able to connect right there in the Cooper Mine, the Chi area and move it right into the Tuba City area.

There are a number of benefits locally as well as nationally, again to improve the economic conditions on the reservation. I think unemployment is around 50 percent.

And this will help bring opportunity for coal development. There are probably two, three hundred, maybe four hundred years of coal in the Four Corners area and we're proposing to build a power plant. We went into a development agreement recently with Stieag Power out of Houston, a German company, and to build a 1,300 to 1,500 megawatt to optimize the use of the NTP.

We have a draft EIS and a final EIS and a record of decision back in 1997. Again, I mentioned the state CEC; we got that in 2000. We have a Navajo Nation right-of-way for the line across trust and fee land. And we have a letter of intent with Transelec. We're negotiating on the terms and conditions right now for a development agreement. We hope to have that by the -- before the end of the year.

What does that all mean? NTP means generation opportunity. We believe that NTP can carry about 1,800 megawatts of new generation from Four Corners into the gas-dominated markets of southern California, Nevada and Arizona. I believe that based on discussions and information I have the gas supply domestically is about 50 to 100 years. Coal supply is probably 200 to 400 years. So when 20 years from now when the gas plants are hurting for gas and the prices are rising we feel that with a base load coal plant we can be very competitive in the gas-dominated market.

We expect to be in service by October '08 with the transmission line. Hopefully will be around the same timeline with the generation projection.

So with that I think with FERC I think we're interested in innovative rates so that the Nation and our partners can be competitive and provide, hopefully, lower cost power through our lines. I know that power flows south from Four Corners and it sort of has a "W" type motion, about 17 or 18 nodes before it gets into California. But with a direct route from the NTP there's only about three or four nodes that you have to hit so there are going to be a lot of pancaking charges that will be eliminated.

And then there are at least three or four interconnection points in the line that will help move power east, west, north and south. So there are a lot of benefits and dynamics to this line.

So thank you for listening. And I'll move it to the next speaker.

MR. GRANT: Thank you, Steve.

And finally with a residential consumer look at these issues, the director of our Residential Utility Consumer Office, Steve Ahearn.

Steve.

STATEMENT OF STEPHEN AHEARN, DIRECTOR, ARIZONA'S
RESIDENTIAL UTILITY CONSUMER OFFICE (RUCO)

MR. AHEARN: Thanks, Mike.

The Arizona Residential Utility Consumer Office is akin to in some other states what's known as a division of ratepayer advocates or an office of consumer counsel. Kind of a very smallish office, kind of lean and mean. We're ten people. We have accounts and attorneys and we derive whatever power we think we have based on to the extent we're able to influence decisions taken by our Public Utility Commission.

Now, I think I have the most easiest and most intuitive perspective to represent here today because each of us at the end of the day when we take off our grey flannel regulator and utility owner suits and go home we become residential utility consumers. And that's on whose behalf I'm speaking today. So it's an incredibly obvious perspective.

Our needs and wants are simple. And I'm going to use the words "our" and "we" and "us" as though I am speaking for these great unwashed and uneducated masses who don't know and probably don't want to know much about what we're talking about here today. Our needs and wants are very simple. And we don't always express them in the most rational way and often we express them in a very contradictory way. We want the lights to come on, we want them to stay on. When they go out we expect them to come

back on right away.

And this expectation is not unreasonable. It's something that's been developed over the last 100 years because this has been our experience, it's worked.

To the extent that we're even aware of utility issues we expect the utilities or the transmission owners to have enough capacity in place to meet growth and all of our anticipated future needs. And if utilities and transportation owners need to build additional capacity that's fine, as long as it's built in somebody else's backyard.

(Laughter.)

As for wholesale markets, RTOs, ISOs and the rest of the acronym soup, these are at best abstractions to us, and at worse a further break from the very comfortable, very familiar integrated system of the past. As such, many of us regard changes as kind of a danger, kind of an exposure to risk that we didn't previously have. We feel more vulnerable about it.

We as a class of residential users purport to be rugged individualists. We claim to embrace market mechanisms and free trade. Furthermore, we loathe monopolies. However, our worshipping at the altar of competition ends where the price volatility and reliability rubber hits the road.

To the extent that the small user class is even aware of these larger economic and political forces that are bringing change to the electric utility industry we don't believe that any of the marginal benefits of the change will even accrue to us. Instead, the big dogs will eat first and we don't expect there to be any table scraps left for us.

Ultimately we reserve the right to scream bloody murder when you're ten years into your very detailed planning processes and we discover it for the first time.

In short, what we want is certainty, certainty of supply at this instant and in the future, certainty of price stability, certainty that meeting the needs of other consumer classes will not disadvantage us as small consumers.

Now, as for big picture notions of regional transmission planning, standard market designs, the surrendering of state autonomy to federal authority, generally we as a class aren't aware of such things. But at least here in the West we kind of knee-jerk respond against what we perceive, perhaps incorrectly but perhaps not, what we perceive to be a power grab by nameless, faceless bureaucrats in Washington, D.C., bureaucrats who of course we believe can't possibly understand the West. We trust our local utility, the homeboys, the local utilities and the regulators and our local elected officials to look out for

our interests.

Now, I think if you could find 100 prototypical residential electric utility consumers who understood such matters a vast majority of them would simply prefer a return to an old vertically integrated system.

So in conclusion, understand that the small user class is relatively uninformed on technical matters but ill at east about changes to a system they perceive to have worked very well over the last century. To the extent that economic and political forces are pushing the system toward greater integration such changes should be guided and informed by the principle of first do no harm.

Thank you.

MR. GRANT: Thank you, Steve.

That's it. Questions? Commissioner Hatch-Miller?

MR. HATCH-MILLER: Thank you, Mr. Grant.

My question is for John Woodley. Interesting thoughts as you expressed them. And what I've been sitting here waiting to ask you is this: can you explain to me kind of so I can understand it why investors would, let's say we're talking about a 500 megawatt plan, a gas-fired generator plant and we have two people building it, one let's say is Salt River Project, able to set its rates and recover directly from an existing customer base versus let's say a merchant plant that's coming in without any existing

contracts, why your investors would prefer the merchant plant over the SRP plant? I don't understand.

MR. WOODLEY: I don't actually think they would. And I hope I didn't necessarily imply that.

I will say this, there's a lot of talk about the rationality and efficiency on the part of investors. And it's actually only true in the long run and in the aggregate. One of the things that was pretty interesting recently was you might have noticed that in effect some of the merchant developers actually had a negative cost of capital.

Now what am I saying there? Basically investors are relatively passive, they sit and they look at past history. So they're going to be seeing a pattern of growth. This was what Enron was trying to project. This is what everybody is trying to project. The minute you interrupt that pattern the stock crashes. And when the stock crashes you can't get money anymore. And that's when the whole thing changes.

But while merchant developers were on that track where things looked like they were growing and growing in a very steady and predictable way they were able to float more stock and get more money and continue to build. So that's why I say they had a negative cost of capital, if they stopped borrowing they were going to lose money.

And it's not right, it's not necessarily rational but it is a function of in my opinion a very poor flow of information. There was a lack of information flow there that investors just didn't see.

And I'm sure I didn't really answer your question particularly well but I think in the sort of standalone basis if someone were to look at the two and ask which one they should invest in they would go with Salt River. If they were asked would they go to the old, for example, AES that used to get a very good and very tight long-term off-take contract with a credit-worthy counterparty they would probably go with AES.

So, you know, it's kind of a question of the facts and circumstances at the time. But in the long run they're going to go with certainty.

CHAIRMAN WOOD: I do want to follow-up on one thing or so, I won't be long. LMP allows you to enter into a long-term contract but flow gates do not. Walk me through that.

MR. WOODLEY: Great question. Sorry I didn't explain that very well.

What we look for in a contract is a high degree of certainty surrounding the delivery circumstances that you're going to be talking about and some understanding as to what the protocol at those delivery points is going to be. If,

and I think we do believe this, we know, we feel that the only stable protocol, the one that you ultimately gravitate to is LMP because points do have fundamentally different value at times.

Then if you try and simplify by aggregating points you end up with a situation where you know that that group of points is going to change over time. And I don't know how to write that contract. You know, what's the delivery point for this contract, for this off-take contract? What's going to replace that delivery point and what's going to impact the value of that delivery point when the protocol changes?

To give you a simple example, of course in Texas even now there's discussion as to what the zonal boundaries are going to be because there is some though, well, maybe we need another zone. Well, of course you need another zone. You're going to need more, you know, need more and more zones as time goes by because as the market becomes more and more efficient you've got to price more and more accurately.

And that type of uncertainty is a type of uncertainty that we have a very difficult time dealing with because we're not sort of fundamental analysts of the system. We don't try and out guess where prices are going. We don't try and actually do much in the way of trying to understand the fundamental system at all. We just observe

what prices are. And we're looking at prices with respect to a particular protocol now. And that protocol is going to change. And I don't know what it's going to change to.

CHAIRMAN WOOD: Steven Begay, are you all, it is an AC line; correct?

MR. BEGAY: Yes.

CHAIRMAN WOOD: Are there interconnections with the existing utility grids along or does it really kind of run -

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MR. BEGAY: It would interconnect in three locations.

CHAIRMAN WOOD: Are there any issues with that that have come up?

MR. BEGAY: I will come up I think. We're going to be filing to interconnect soon once we finalize the development agreement with Transelec. So they'll take the lead in making the applications for interconnection.

CHAIRMAN WOOD: And, Dennis, you had mentioned something about ADR, and I just want to follow up on that. What is that in response? Is there something that's happened out here that kind of informs that a little bit?

MR. DELANEY: No. It's probably more of a fear.

CHAIRMAN WOOD: Okay.

MR. DELANEY: That we just need to be sure that the models are well defined and we understand the impacts of an

LMP model if that's where this region goes. We want a chance to be heard.

CHAIRMAN WOOD: Let me just ask, all of you kind of come from a different perspective from each other as well as from the last panel. But one of the issues that certainly Nora and Bill and I have been grappling with for two years along with our staff and a lot of the western market participants in a design in California that has gone forward and is even now going into a different realm. And you all in the adjacent but interconnecting markets are staying in kind of a premarket design world.

California can and will go forward with whatever, you know, it comes up with and we sign off on, but how do you envision as market participants as really the I guess one of the big centers of load here in the West go forward with a market design how do you all envision 2000, 2001 not happening all over again if we don't get some construct built around all of this?

That's why we're here folks, just to kind of draw the line here.

MR. HUHMAN: I'll take a crack at that.

Obviously as a generator and power marketer we would prefer that all the markets be in harmony. And there's the innumerable seams as people have talked about obviously are there. At the same time I think you already

have that situation, you have a much more sophisticated market in California than you have outside the California WECC. And power clearly does move from California ISO out, both out and in.

So there are ways to work around it. The question is how much inefficiencies do you build in when you're not having essentially the same system, regardless of how much work you put in to try and resolve your seams issues?

As regards to how do you prevent a 2000, 2001, I might ask a clarifying question. I think of 2001 as really have two interrelated but separate problems. We had a financial problem and then we had a physical resources problem. Were you thinking more of the financial issue or the physical resources shortfall? The second one?

CHAIRMAN WOOD: Both.

MR. HUHMAN: Both of it.

It's always been my view that the financial problem could have been solved very simply if you put yourself, take a little thought exercise and put yourself back in the first quarter of 2000 before there were problems and if you said what if the load serving entities had all had supply portfolios based on the sound risk management principles? At that point in time even if the prices spiked totally unfettered by any sort of price cap the financial damage to those entities which were intermediaries would have been

minimal and probably none of that would have been passed on to consumers.

So if you're asking how do you solve the financial problem I simply think it's based on getting ourselves positioned so that all the supplies build sound supply portfolios.

The physical problem I think was on its way to being solved. We were a little bit unfortunate in our timing. If you look at what happened in California, nobody built any power there for a number of reasons for a long time at least in part because people were anticipating that something was going to happen even before, even if they didn't know exactly it was going to be A.B. 1890. And I think the utilities didn't want to build, merchants were not ready to build because they didn't know what their structure was.

But once you had A.B. 1890 built all of a sudden tremendous numbers of power plant projects were in the pipeline towards being permitted. And those things were tooling along. And, unfortunately, the physical shortages, you know, the perfect storm situation happened in 2000 and 2001 before all of those plants were in the pipeline and were completed.

If the same physical conditions had happened I say two years later after a lot more of these projects had been

permitted and had been constructed and you had those resources online, certainly the problem would have been reduced or perhaps not even have happened from a physical perspective.

And I think that was really just the unfortunate nature of the transition from the integrated utility model you had in California to the I guess California really took a much more radical approach than anyplace in the country that I'm aware of where they mandated that their investor-owned utilities divest themselves of most of the generation. And we had a transition gap while people were waiting to see what would happen.

I think that ties back into John's concern, you know, the thing that investors hate the most is uncertainty. If we get certainty, and that means both at the federal level and at the state public utility commission levels because they clearly have a very great impact on the situation as well, I think we'll get back into an equilibrium situation and you'll see plenty of resources built and I think you'll see plenty of transmission built.

And maybe that's a bit of Polyanna view, you know, sort of hoping that if you set the rules right they'll build it and they'll come. But I really think the problem is sort of self-solving once you return to a stable situation of market, for both market and regulatory environment.

MR. WOODLEY: I'm not going to be probably as good as Steve was but I generally agree with him. First of all, I think I probably should just go back and clarify one of the things I said before because it's important in the context here.

When I said it's not possible for us to offer a contract in a certain circumstance what I mean is that it's not possible to do it at the same price with the same economics. So I suppose really you're always talking about a matter of degree. I should never be as strong with words as I was there.

And that really goes to what I was about to say here with respect to structure. I would agree, it is not optimal that California is going this alone. Even if it does go right it's not optimal and it's going to be more costly than it would otherwise be. I'm convinced of that.

How, the next question being how would you prevent something like what happened in those years happening again? I think Steve just put that all extremely well. There's a few points that I would like to add.

Structurally the original California market I think was designed as a big bet. I mean maybe that's not a politically correct thing to say but it really was. Fundamentally everybody knew that when you deregulate prices go down. And the things that you don't want to do when

prices go down is you don't own generation so you make yourself divest of it.

You want to make sure that you don't lose your retail customers so you give them a discount and you collect your stranded costs through contracts that make it difficult to take it away.

And you don't allow yourself to enter into long-term contracts because those are going to be stranded assets.

Well, that's a bet. It's happened many times before. It's going to happen again. It happened in Orange County, it happened with Berings Bank. And the outcomes sometimes are very wonderful and sometimes quite disastrous.

So in effect I would just say that Steve's point as to the supply portfolio is critical. I would add, though, that they didn't need to have that in the former power plans. If they had been allowed to or required to hedge their retail exposure they wouldn't have had the problem that they had.

And then I would like to add one final thing which is still a mystery to me. It is a complete mystery to me why when the entire region experiences these high prices why it's an entity that you would expect to be a model of bureaucracy and slowness to act, the Bonneville Power Administration, that leads the way in buying back power that

it had sold under long-term contracts in order to cause demand to go down? Why it's them and no one else? And particularly not why -- you know, IOUs, it should be much more innovative and much more fast to act. That's a very surprising thing to me.

Great incentive for demand-side management. There was demand-side management practiced by some. Why was it not practiced by others?

MR. DELANEY: I don't have a real good answer for you. But the fear of what happened in 2000 and 2001 is very real to the small entities in Arizona. The majority of the ACES members survived that crisis mainly out of just being lucky.

What we're doing now is planning and making sure that we're protected that if it does happen again that it's localized and it doesn't impact our direct consumers. But we're also worried about the WestConnect or an LMP model having those types of impacts here in the Southwest, not just confined to the California area but the whole region. And that's a real concern for us. And maybe it's we don't know enough about it. But --

CHAIRMAN WOOD: If LMP weren't part of that are you still worried?

MR. DELANEY: We're still worried about just the cost of the RTO.

MR. ELLISON: Let me just say two things, first of all that I, you know, I agree wholeheartedly with both Steve and John. And I thought they very eloquently described what I would have said in response and not as well in response to your question.

The only other thing I would add is that there were a variety of complex reasons that generation was not added commensurate with load in the 1990s in California. But that was certainly a contributing factor to what happened there. And I would remind everyone that that generation was not added under the prior regulated regime that a lot of people want to go back to.

MR. BEGAY: This is Steve Begay, DPA.

Real quickly I think a couple of things. One is diversity of fuels. I think if it's gas dominated, you know, as the price goes up everybody's in the same, same game. But if you have fuel diversity I think it helps to have coal and other types of, other fuel power that you get I think that helps.

And then California being an island on its own I think that's a problem in itself.

And then the ability of the power to flow freely during seasonal variations, in other words if the COB lines are full I think there ought to be a way to move power down the western or the eastern side of the donut as people call

it. And I think that's where the NTP could be a real help. If you can't move power from hydro sources into northern California you ought to have another route. And I think NTP will be a real help in that case.

MR. AHEARN: I can't improve on the comments of the first two speakers. I thought they were very eloquent and if I would have been able to say it as well I would have said it precisely that way.

CHAIRMAN WOOD: All right.

MR. GRANT: Okay, thank you very much.

CHAIRMAN WOOD: Good, we do have still a good group. I'm sorry, I was sitting in the front and didn't turn around.

At this point we'd like to invite folks in the audience if you've got any just ideas to offer, comments for the broader consideration or questions of anybody who was on an earlier panel that may have kind of crept into your mind here late in the day, give you an opportunity to do that. We do have a public record going on here so we want to always entertain and welcome thoughts of really any nature at this point to kind of add to the mix.

MR. BAGLEY: My name is Ken Bagley and I didn't come actually with any prepared comments. But one of the concerns I have then, I'll just say I'm one of the few here, I know of one other who has the pleasure or displeasure of

having degrees in both engineering and economics so we get to deal with both sides of this. But in my mind one of the main disjoints that occurred in California was the fact that the market really didn't deal with the retail side. What happened in California when the price went to \$300 or above wasn't reflected to the retail customers.

And I think that's an important thing for both the federal as well as the state regulator to realize is the need to coordinate because you can't have a market that deals just from the generator to Palo Verde or to COB, it has to incorporate all the way down to the meter so that you have the entire influence of that market.

MS. MCKINLEY: Anyone else?

CHAIRMAN WOOD: Anybody else?

PARTICIPANT: What has been your experience trying to involve residential users or the non-technical in housing, how do you -- have you had any luck trying to translate this very complex subject to everyday?

CHAIRMAN WOOD: That's a great question. What we're trying to do, I mean I was a retail regulator too, as all my colleagues up here. Quite frankly the mandate there is to have a direct relationship with the retail customer. Ours is to make sure that the parties in between the utilities, the competitors, the alternative suppliers and the wind people, the transmission people, the financiers,

what have you, kind of have some stable rules so that they can generate some benefits that these customers can have.

I characterize the two-part level competition as wholesale competition is what we're trying to facilitate here. And the reason we're here, and because we are thrilled about it, I'm thrilled to be in Arizona, don't get me wrong, but because there's more than one state involved. It's multi-state so we're here.

Now, if the federal capital were in Albuquerque or Denver or here in Phoenix I guess it would be different. But unfortunately, and I'm speaking this as a Texan, it's way over on the wrong coast. Got to deal with that.

But that's why we're here and we're trying to facilitate as part of our mandate under our statutes the creation of just and reasonable rates at the wholesale level, so between and among utilities and market participants. That's an economic decision. It's a decision based on the economics of having realtime competition between and among the various generators of electricity because really that's where 70 percent of the end use customer's bill comes from is that generation component.

And only until about 20 years ago was that deemed to be a monopoly. Since that time you've had numerous generators of all types, big and small, new technologies coming in that want to play in that market and quite frankly

want to bring value to customers in a way that utilities have done for many years.

So the addition of that to that 70 percent component of your bill is what really our mandate is to try to facilitate.

The political decision is one that state legislators or I believe in this state you folks can make directly at the Commission which is a great gift, or challenge I'm not sure, perhaps both, that a political decision then about, okay, if there are benefits of wholesale competition, and I think the studies have shown that despite the California experience in every other market there have been -- there was a great study put out yesterday I think on the TJM experience which is probably the most nature of the markets we have here that showed \$3 billion of savings last year, 2002. It was an interesting and pretty well-resourced study -- how then do those benefits get into customers' pockets?

That's a political decision. Do we have that done by a regulated setup as most states have been up until at least recently or do we allow a market to allocate those resources?

Or, as I think is becoming probably the paradigm that the country will most likely move toward that there would be kind of a core/non-core split where the larger

customers, much as we've seen in natural gas, the larger customers will go out and play in the marketplace and that there will be a regulated entity for most if not all of the smaller customers, ones you represent. So that then those benefits were kind of allocated through more of a pro rata, more regulated mechanism. We call that the Oregon model. When we were in Texas we called that the Louisiana model because that was being proposed for Louisiana at the time.

So I, you know, I think the levels of competition what we deal with is really trying to facilitate and make most efficient and most, again the reduction of transaction costs that I heard this gentleman talking about, we're trying to make sure those, that they're gains for the customer in the first place.

If those can be obtained, and I think evidence has shown that that can happen clearly in most regards in this country, then how do those get to customers? And that's really where the partnership has got to work so that we set up in the first place the place where we can get some winnings. And then the second place is really a state decision on how to divvy up those winnings to the customers or the voters.

So this is a forum where I do think we'd get less of that because as you state as articulately as I've heard in a long, long time, the customer doesn't care, they just

want it to stay on. They don't want to have to reset the VCR more than maybe once a year. Unless you have five-year-olds, they really like to do that for you for free. And they want it to be maybe cheaper than last year or at least as reasonable as it was. Or if it goes up, a real good reason why it went up like gas went up, and hopefully it will come back down.

That is what I heard six-and-a-half years as a Texas regulator. I hear that not quite as loudly as I do because I'm unfortunately farther away from all that now. But in setting this up that's what we try to do is try to make sure that we get the bright people, the different perspectives.

I appreciate the assistance we had from our colleagues here at the state to put together a nice diversity of viewpoints today. But you heard them. I mean I have to say the panel of those who have and those who want to add to it was kind of a stark contrast this afternoon but probably actually more contrasting than we've seen at any of the conferences, including that in the Southeast, which is, you know, an issue I think we're all going to have to work with as to what do you all really want to have happen out here.

The growth in this part of the country is as significant economically as I think anywhere from the

statistics I've seen. And I'm sitting in probably the ground zero of that effort. And but yet Arizona is not an island. I know you'd all like to be after what happened to California, it would be fun to be, but there are interconnection issues here. And we certainly want to provide a platform that that can happen and happen well.

And, again, please consider us your allies and colleagues in that effort. We want to help that benefit for New Mexico, Arizona and the other neighboring states be maximized through whatever collaborative efforts we can do. I want to again dispel and we've tried to do in now the seventh of these issues dispel the great myth that there is some super battle set up here between states and federal. We're all working for the same people. The same people that vote you in are the same people that vote in members of Congress who confirmed me and confirmed her. So we just had a few more other people involved in that mess and we have to work for all of them as well.

So I know we're all just trying to do our jobs. And I want that to be from our perspective please know friends and colleagues on the Commissions and staff and market participants that that's an effort that we want to do honestly and collaboratively with you all here in the Southwest.

There is a lot I think of ground to cover. And I

don't want to profess to be very articulate at the end of a long day of listening intently to everything everybody said other than to say thank you. We'll be back. We want to continue to stay engaged in the effort out here.

I think I want to just say on a personal level I would hope we don't miss some opportunities out here. You've got a lot plus, plus, plus going on out here. And clearly the goal here should not be to make that any less than it is today. But I would hope that ten years from now people look back and say, you know, all those folks who were in that room at that hotel at that time started something that went in a very positive direction and brought a lot of benefits to customers that live and work out here rather than just kind of stay where we were in 1997 when I first got a briefing in my office in Austin on the DesertSTAR initiative by our friends at El Paso Electric coming by to tell me about it.

It hasn't really improved since then. And I hope we aren't still worrying about that in another seven years. We'll work our best to make sure it moves forward because I think it does. This part of the country deserves it because it's going to be the dynamo for our national economy I'm sure for the next 10 or 20 years or longer.

Thank you all for your time. And I appreciate the hospitality of this fine hotel and this wonderful state.

Have a good afternoon.

(Whereupon, at 3:41 p.m., the conference was concluded.)

